
# Japanese Contract and Anti-Trust Law

## A Sociological and Comparative Study

WILLEM M. VISSER 'T HOOFT

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RoutledgeCurzon
Taylor & Francis Group

The text of this book was defended as a PhD thesis on March 22nd, 2000, Leiden University.

First Published in 2002
by RoutledgeCurzon
11 New Fetter Lane,
London EC4P 4EE

Simultaneously published in the USA and Canada
by RoutledgeCurzon
29 West 35th Street, New York, NY 10001

This edition published in the Taylor & Francis e-Library, 2005.

"To purchase your own copy of this or any of Taylor & Francis or Routledge's collection of thousands of eBooks please go to www.eBookstore.tandf.co.uk."

*RoutledgeCurzon is an imprint of the Taylor & Francis Group*



*British Library Cataloguing in Publication Data*
A catalogue record for this book is available from the British Library

*Library of Congress Cataloguing in Publication Data*
A catalogue record for this book has been requested

ISBN 0-203-39838-6 Master e-book ISBN

ISBN 0-203-39973-0 (Adobe eReader Format)
ISBN 0-7007-1577-0 (Print Edition)

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# Acknowledgements

First and foremost I would like to express my gratitude to the late Prof. A.A.G. Peters who was my supervisor when I started this research in 1993. He was a great inspiration to me. His enthusiasm for the study of Japanese law motivated me to pursue this research. His proposal that I conduct a few in-depth case studies in Japan has indeed proved to be very rewarding.

With the financial support of a two-year scholarship from the Japanese Ministry of Education I was able to conduct my research at the faculty of law of Tokyo University from 1993 to 1995. I am profoundly indebted to Prof. Yoshihisa Nōmi and Prof. Takashi Uchida who were my supervisors during this period. For the many stimulating discussions with them, which were very helpful in developing my research questions, I am very grateful. I also wish to express my appreciation for the assistance that I received from many other staff members of the faculty of law of Tokyo University.

In particular, I would like to thank Mitsuo Matsuzawa (the General Editor of the Commercial Law Centre) who assisted me in my field research into the termination disputes within the Japanese distribution system for luxury cosmetics. Through his numerous contacts he was able to arrange the many interviews I conducted in Japan. Without his assistance these interviews would not have been possible. Furthermore, he continuously provided me with much of the necessary Japanese legal material. And, of course, I would also like to express my sincere appreciation to all those I interviewed in Japan.

A grant from the Isaac Alfred Ailion Foundation enabled me to continue my research at Leiden University and to return to Japan during November 1997 for the second part of my field research.

I would also like to acknowledge the support I received from the Dutch law firm, Trenité van Doorne, where I worked as a part-time employee from 1996 to 1998. Their strong interest in my research was very stimulating. They also provided numerous opportunities for gathering information on Dutch law and practice, which enabled me to bring my research in Japan into perspective.

I also wish to express my gratitude to the practicing attorneys G.van der Wal and R.F.K.Visser who provided invaluable information about the termination disputes within the Dutch distribution system for luxury cosmetics.

I am very grateful to Nobuko Karthaus-Tanaka who corrected my correspondences written in Japanese. And I thank Peter Morris who was very helpful in proof reading and correcting my English.

Last but not least, without the strong support and encouragement of my wife, Lucie, I would never have been able to finish this study.

# List of abbreviations

| | |
|---|---|
| BGB | Bürgerliches Gesetzbuch |
| ECLR | European Competition Law Review |
| ECR | European Court Reports |
| FTC | Fair Trade Commission |
| FTI | Fair Trade Institute |
| HR | Hoge Raad (Dutch Supreme Court) |
| *HR* | Helena Rubinstein |
| KG | Kort Geding |
| LDP | Liberal Democratic Party |
| Minshū | *Saikō Saibansho Minji Hanrei shū* (Collection of Civil Cases of the Supreme Court) |
| MITI | Ministry of International Trade and Industry |
| M&M | Markt & Mededinging |
| NJ | Nederlandse Jurisprudentie (Dutch Law Reports) |
| NJB | Nederlands Juristenblad |
| NTBR | Nederlands Tijdschrift voor Burgerlijk Recht |
| o. c. | op. cit. |
| OJ | Official Journal of the European Communities |
| p (p). | page (s) |
| PRG | Praktijkgids |
| Rvdw | Rechtspraak van de Week (Dutch Law Reports) |
| SEW | Sociaal-Economische Wetgeving |
| TVVS | Tijdschrift voor Verenigingen, Vennootschappen en Stichtingen |
| v. | versus |
| Vol. | Volume |

# 1
# Introduction

## 1
## THE JAPANESE INTEREST IN CONTINUING DOMESTIC TRADE RELATIONSHIPS

Since the beginning of the 20th century, starting in the 1920s, there has always been a strong interest in domestic continuing trade relationships *(keizokuteki torihiki)*[1] among legal scholars and practitioners in Japan. In the first 20 years there had been much influence of German legal doctrine upon these scholars.[2] During that period the labour and lease contract were the main representatives of continuing contracts. Yet, their interest was not so much based on practical cases. It was not focused on the actual condition of these relationships, but rather on general theory. There was mostly a theoretical interest in continuing trade relationships.[3]

In contrast, particularly since the 1960s, many Japanese scholars and practitioners became more interested in Japanese 'living law' and more empirical research was conducted on commercial relationships within the distribution sector. For this reason, many of these scholars started to gain more interest in distribution agreements as one type of continuing

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1 Continuing contracts can be structured in a variety of ways: 'long-term' contracts with stipulated, periodic deliveries and payment; long-term master contracts under which a series of subsidiary, independent sales are made; open-ended contracts with an alternating series of obligations; or a series of orders placed with a transaction partner on the same terms each time, within a trading relationship.

See Veronica Taylor (1993), 'Continuing Transactions and Persistent Myths: Contracts in Contemporary Japan', 19 *Melbourne University Law Review* 371.

2 German legal doctrine had a strong influence on Japanese civil law after the enactment of the Japanese Civil and Commercial Codes at the end of the 19th century. They were drafted largely along the lines of the German Civil and Commercial Codes.

3 Takashi Uchida (1997), *'Keizokuteki torihiki ni kansuru jisshōteki kenkyū no mokuteki to igi'* (The Meaning and Purpose of Empirical Research in Relation to Continuing Trade), 627 *New Business Law* 6. For a list of these Japanese studies, see Hiroyasu Nakata (1994), *Keizokuteki baibai no kaishō* (The Termination of Continuing Trade), p. 20–24.

4 H.Nakata (1994), Ibid., p. 28,44.

commercial contract. This was also triggered by the growing number of termination disputes concerning distribution agreements which received their attention.[4]

Of a slightly different nature is the recent focus in Japan among legal scholars and economists on continuing commercial trade relationships and Japanese trade customs *(nihonteki torihiki kankō)*. During the period of great economic growth in Japan there had already been an interest in these customs, but particularly the recent trade problems between Japan and the US have caused this interest to becomemuch stronger than previously. During the Structural Impediment Initiative (SII) talks between the US and Japan which started at the end of the 1980s, the US negotiators criticised Japan for its traditional transaction practices and also argued that continuing commercial contracts in Japan were an invisible trade barrier which prevented new market entrants from establishing business in the distribution sectors of the Japanese economy. They further contended that continuing contracts are a means by which unfair competition devices such as resale price maintenance and rebates are established and that such practices are seldom made explicit in the terms of the contract.[5]

Although some disagreement exists in Japan among legal scholars and economists about what exactly constitute Japanese trade customs, they all agree that it is the existence of many enduring trade relationships in Japan which enhances the use of these Japanese trade customs. Many recent economic studies concerning Japan also point to the fact that continuing transactions are integral to the operation of Japanese-style capitalism.[6]

The legal scholar Takashi Uchida indicates that so far among the Japanese there have been three ways of discussing continuing trade relationships in Japan.[7] In the first approach the distinct nature of the Japanese preference for continuing contracts is emphasised and explained by Japanese culture. Several Japanese legal practitioners pointed out that in Japan

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5 See Veronica Taylor (1993), op. cit., p. 364.

6 T.Uchida (1997), o. c.,p. 6–7.

7 Ibid., p. 7–8.

8 For example see Kenji Iwaki (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction) *Zadankai* (Round Table Discussion), 560 *New Business Law* 10. Non-Japanese such as the British sociologist Dore have asserted that opportunism may less often threaten the integrity of a deal in Japan and have emphasised the prevalence of moralised trading relationships of mutual goodwill in the Japanese economy. Dore also argues that the continuation or extension of these relationships has strong moral connotations in Japan. See Ronald P. Dore (1987) *Taking Japan Seriously–A Confucian Perspective on Leading Economic Studies,* p. 173–182; Also R.Dore (1983), Goodwill and the Spirit of Market Capitalism, 34 *The British Journal of Sociology* 459–82; R.Dore (1986), *Flexible Rigidities,*

9 Many Japanese have argued that under certain conditions the preference for continuing transactions can be explained rationally. See for example Motoshige Itō (1992), 'Organisational Transactions and Access to the Japanese Import Market' in: P.Sheard (ed.) (1992), *International Adjustment and the Japanese Firm,* p. 50 and P.Sheard, 'Introduction', in P.Sheard o. c., p. 5. The theory of economist Oliver Williamson had much influence upon them. See O.E.Williamson. (1986), *The Economic In*

continuing or extending a continuing trade relationship has strong moral connotations, which means that one party to the contract cannot easily back out of a continuing contract.[8]

A second approach, which has recently gained strength, explains the economic rationality of continuing contracts. Because it emphasises the universal nature instead of the uniqueness of Japanese continuing contracts, it functions as the antithesis of the first cultural approach. A preference for dealing on a long-term basis is not seen as a cultural peculiarity but rather as a rational risk-minimisation strategy. Continuing transactions have an internal logic and for this reason they are also common in many other modern industrialised countries.[9]

A third approach, which is adopted by legal scholars, distinguishes itself by its strong emphasis on the distinctive features of continuing contractual relationships in contrast to the one-shot deal envisioned by classical contract law in the Civil Code. Generally speaking, the growth of contract types such as distributorship agreements has strengthened the view among many Japanese that the paradigm contract in Japan is not this one-shot deal but a continuing contract. These scholars especially focus their attention on the problems caused by the termination of continuing contracts, such as whether the termination is retrospective, whether an advance notice period is required and whether termination is valid without good reason. One type of contract commonly described by these scholars has been the distribution agreement.

## 2 DISTRIBUTION AGREEMENTS, DEFINITION AND TERMINOLOGY

When Japanese manufacturers wish to sell their products they have many possibilities. In most cases they appoint independent merchants to resell the products to other wholesalers, retailers or ultimate consumers.[10]

There is no codified legal definition in Japan of a distribution agreement. Moreover, it is difficult to give a clear definition of a Japanese distributor. These independent traders are usually called *tokuyakuten, dairiten* or *hanbaiten*.[11] The exact definition of the word for distributor, *tokuyakuten,* which is used most frequently, is not very clear. The vagueness

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*stitution of Capitalism: Firms, Markets, Relational Contracting.*

10 See Yoshinori Hosoya assisted by Anthony Zaloom (1992), 'Agency and Distributorships', in: Zentarō Kitagawa (ed), *Doing Business in Japan,* Volume II, Chapter 5, p. 4; for the variety of distribution agreements in different industries see Kenji Kawagoe (1996), *Hanbaiten keiyaku no handobukku* (Handbook of Distribution Agreements), p. 293.

11 However, there is no clear distinction between them in commercial usage and they usually mean the same. See about these different terms: Kenji Kawagoe (1988), *Keizokuteli torihiki keiyaku no shūryō* (The Termination of Continuing Trade Contracts) *New Business Law (Bekkan)* (Separate Volume), Vol. 19, p. 5–6.

12 H.Nakata (1994), o. c., p. 48–49.

13 See Y.Hosoya assisted by A.Zaloom (1992), o. c., p. 6.

surrounding this word is caused by the various expressions used in actual business, in legal discourse and judicial decisions. Furthermore, in trading relationships between manufacturers and distributors the contents of the actual trade are also sometimes not very clear.[12] Usually, it is not the name which parties give to the contract that is determinative, but the actual circumstances of the trade. Generally speaking, a distributor is an independent trader who sells the products of his supplier in his own name and for his own profit.

In Japan the term distributorship is commonly used to describe a sales representative who purchases products from the supplier for resale to other wholesalers, retailers, or the ultimate consumers, with the ownership right to the goods usually passing to the distributor at the time of delivery of the products.[13] The essence of a distributorship is not the mere repetition of purchase and sale of the principal's products, but rather a grant to the distributor by the principal of the right to sell the products of the supplier and a continuous supply to the distributor by the supplier of its products to effectuate such a sales right.

It is very difficult to discover a brief and clear definition of a distribution agreement in Japanese legal material. Most Japanese legal scholars only describe the characteristics of this agreement without providing any brief definition. Based on these descriptions I use the following definition of the distribution agreement:

An agreement whereby one party, the distributor, agrees to purchase and resell in his own name and for his own account products and/or services of a certain company on a continuing basis and agrees to co-operate with the marketing policy of that company. In turn the company, or its importer or higher-level distributor, agrees to sell and supply these products and/or services to the distributor.

Although ownership and control generally rest with the individual distributor, it is still very susceptible to the control exercised by the manufacturer or higherlevel distributor, often because of the terms of the distribution agreement. Although both parties are mutually dependent, they are not equal. There are differences in economic power and social status, which are also characteristic of distributorships in other modern industrialised nations.

Generally speaking, I assume that distributorships in Japan share many common characteristics with distributorships elsewhere.[14] It must be noted that distribution agreements often represent a highly developed form of retailing in which a product or service is bundled together with an efficient delivery system. Distributors purchase not only the products themselves but also expertise and management advice. Producers choose distributors who will promote the product as if it were their own. Therefore, they also need to control the quality of service offered by the distributor. The value of the trademark must be maintained by providing the products and services in the agreed manner.

## 2.1 Standard Patterns in the Phrasing of Distribution Agreements

These agreements are usually standard-form. Typical clauses of a distribution agreement are the following:[15]

First, there is usually a clause which formally appoints the distributor as a *tokuyakuten* of the manufacturer's brand. In addition, there are clauses, which stipulate that the distributor shall endeavour to expand the sales and they furthermore oblige that distributor to provide information about its customers to the manufacturer. The standard-form contracts also usually impose duties upon the distributor as to how to use the trade and service marks.

These contracts may also contain provisions for minimum annual purchases or resales. Sometimes these provisions are imposed in the form of a legal obligation but in most cases they are only included in the form of targets which the distributor shall endeavour to reach *(doryoku mokuhyō)*. Occasionally, the contracts set out the limits on the amount of credit extended to the distributor but in most cases the manufacturers do not wish to clearly express these limits.

These contracts may also include non-competition clauses and sales territory clauses which make the contracts exclusive. The more exclusive the transaction the more interdependent the parties will be. Finally, typical clauses are those in which the manufacturer shall provide the distributor with information about the products and the market, shall cover part of the advertisement costs and shall train the distributor's personnel.

In most cases these standard-form contracts also set out the contract period and include automatic renewal clauses. Furthermore, they usually include intermediate termination clauses, which entitle one of the parties to cancel immediately in case important obligations are not honoured by the other party.

## 2.2 Franchise Agreements

A special distribution agreement is the franchise agreement where the manufacturer exercises the most control over the distributor.[16] In the franchise agreement the 'franchiser' usually has almost unlimited decision-making authority over the 'franchisee'. It provides the marketing concept, product ideas and design and develops procedures for delivering the products. In return for the payment of royalties franchisees may utilise the 'bundled' services and/or products provided by the franchiser which are to be resold under a certain image which is determined by the franchiser. It must be noted that franchising systems have increased very rapidly during the 1990s within Japan.[17]

## 2.3 Differences with other Agreements within the Japanese Distribution Sector

Finally, it is important to distinguish the distribution agreement from the commercial agency agreement *(dairishō keiyaku)* and the consignment sales agreement *(itaku hanbai keiyaku)*.

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14 See also V.Taylor (1993), o. c., p. 372.

15 Kenjirō Egashira (1992), *Shōtorihiki hō* (Commercial Trade Law), p. 207–209.

First, a commercial agent refers to an independent trader who makes repeated sales of products of his principal. He has no ownership right to the products he sells and he does not purchase products from his principal. He sells products for the account of his principal and in return he receives a commission from his principal. In general, from the standpoint of termination the difference between distribution and agency agreements is that the amount invested by an agency in its business and in promoting the principal's products is likely to be lower than the amount invested by a distributor.[18]

Second, the consignment sales agreement differs from a distribution agreement in that the buyer, usually called a commission agent *(toiya),* sells the goods in his own name but for the account of the producer. The producer consigns the goods to the buyer but retains ownership of the goods. Where goods remain unsold, these can be returned to the seller at no cost to the buyer. The producer bears the market risk and in addition he must pay a sales commission to the commission agent. The latter is a consignor in relation to the supplier but a seller in relation to the purchaser.[19]

Important factors demarcating the distributor from the commercial agent and commission agent are not the commercial usage of the name of the entities or the name of the contract but the legal factors, such as for whose account the trader sells the products, who bears the loss for unsold products, who retains the title to the products and what he receives as his income.[20]

Several Japanese legal practitioners have pointed out that distribution agreements are far more frequently used within the distribution sector for selling products than commercial or commission agency contracts.[21] Moreover, terminations of such agreements have not caused as many disputes as terminations of distribution agreements.

## 3 UNILATERAL TERMINATION OF DISTRIBUTION AGREEMENTS

In such a highly competitive economy as the Japanese one terminations of distribution agreements or the halting of supplies have occurred frequently.[22] In most recorded cases it concerns manufacturers who cancelled these agreements. Sometimes this led to litigated termination disputes, which have been analysed in detail by many Japanese legal scholars. These disputes especially involved medium and small-sized companies who usually terminated in a more abrupt manner than large manufacturers leaving the distributor no option but to litigate.[23] By contrast, in only a limited number of cases have distributors cancelled the agreement with the manufacturers. Although these may have led to some termination disputes they fall beyond the scope of this study. I decided to focus on the

16 See also K.Egashira, Ibid., p. 203.

17 See for recent figures: M.Sugawara, J.Imai, and K.Hosoda (1999), *'Furanchaizu no mirai'* (The Future of Franchising) in: *Nikkei Business* 24 May 1999, p. 22–33.

terminations by manufacturers since these are much more frequent and lead to more problems than terminations by distributors.

In recent years frictions between manufacturers and distributors have increased. Recently, there have been significant pressures both to lower prices and to restructure distribution channels in Japan. This has put a greater strain on many continuing commercial contracts, which have been described so extensively in Japanese literature.[24] Economic pressures have not only caused further restructuring of distribution systems and subsequent terminations of distribution agreements by manufacturers, but also a greater volume of termination disputes.

### 3.1
### Recent Causes for Unilateral Terminations by Manufacturers

The most important factor is the current recession. After 25 years of enormous economic growth,[25] at the end of the 1980s the 'bubble' economy had well and truly burst. This caused a long period of stagnant economic growth which started in the early 1990s and led to the current recession. It has left Japanese consumers with less purchasing power than before. Therefore, pressures to sell at lower prices have increased, even leading to deflationary pressures throughout the economy. This has in turn triggered the sudden growth of discounters in the 1990s which had many repercussions in the distribution sector.[26]

Although there may be examples of manufacturers and distributors working even more closely together in the current poor economic climate in order to survive, the exact opposite also occurs. While trust in one's business partners and standards of co-operation may work in good times, they cannot always be counted on when the economic tide turns.[27] The current turndown has particularly struck small businesses such as distributors. Large companies have cut back on distributors and have sometimes stopped providing goods to them. The distributors face hard times and sometimes even bankruptcy and have increasingly sought the help of the civil courts, since they no longer feel obligated to their long-term partners who have abandoned them for several reasons.

Increasingly, lawsuits for specific performance and claims for damages for breach of contract are being filed because of financial losses. Facing the possibility of recovering a

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18 Yasuzo Takeno (1997) in: Agustm Jausàs (ed), *International Encyclopedia of Agency & Distribution Agreements,* p. 169.; Also R.Christou (1996) (ed.), *International Agency, Distribution and Licensing Agreements,* p. 489.

19 This transaction type is usually identified as a traditional contracting practice and is currently gradually decreasing. See also about this transaction type V.Taylor (1993), o. c., p. 364–367.

20 Yasuzo Takeno (1997), o. c., p. 167.

21 Ibid., p. 168; K.Kawagoe (1988), o. c., p. 10; K.Egashira (1992), o. c., p. 205–206.

22 For example, see Kenji Iwaki and Noboru Kashiwagi (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction) *Zadankai* (Round Table Discussion), 560 *New Business Law* 8–10; See also V.Taylor (1993), o. c., p. 357.

23 See Kenji Iwaki (1995), o. c., p. 10.

loss in legal proceedings can outweigh the disadvantages of litigation. They may have invested heavily in the relationship. Furthermore, poor economic conditions decrease the possibilities for a compromise since the parties have less leeway (extra cash) for such a compromise. They prefer to risk litigation rather than settle.[28] Special reference needs to be made to the fact that the recession and the resulting decrease in consumer demand has recently caused a great number of disputes within the rapidly growing franchise industry. There has been much friction in the relationship between franchisers and franchisees which has sometimes led to termination disputes.[29]

Another economic factor, which increases pressures upon the distribution sector, are the efforts for more deregulation starting in the 1990s. This increases competition and the need for manufacturers to restructure their distribution systems.[30] A good example is the replacement of the 'Large Scale Retail Store Law' by a more lenient law which enhances the possibilities for opening large stores. It needs to be added that these factors enhance the possibilities for foreign companies to start business in Japan, which only increases with the competition within the distribution sector and the resulting restructuring.[31]

Finally, a third factor increasing pressure on the distribution sector and resulting in more termination disputes is of a legal nature. This is the stricter enforcement of the Japanese Anti-monopoly Act which is, in part, attributable to outside pressure from the US As will be explained below the stronger enforcement of the Act has also triggered more distributors to take legal measures after the distribution agreements have been terminated. Furthermore, it is necessary to refer to the current re-evaluation of the exemption system under which certain products were exempt from application of the Anti-monopoly Act provisions relating to resale price maintenance. For an increasing number of products the exemption from these provisions has been eliminated.

It must be further noted that all the above-mentioned factors also exert pressure on many trade customs which created much mutual dependency and which were widespread during the long period of high economic growth. These include rebate programs; quoted price or

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24 Kenji Kawagoe, Kenji Iwaki, Noboru Kashiwagi and Kōji Shindō (1995), o. c., p. 4–19.

25 I have not compared the situations in times of previous recessions, but the current recession is the worst since World War II, resulting in more pressure on continuing contracts than previously.

26 Kenji Iwaki explains that the growth of discounters forms the third and most influential revolution in the Japanese distribution sector since World War II. It has had more impact than the rise of supermarkets or convenience stores which are considered to constitute the first and second revolution within the distribution system. See K.Iwaki (1995), o. c., p. 7.

27 See for a good example: Michael Gerlach (1990), Trust is not Enough: Cooperation and Conflict in Kikkoman's American Development', 16 *Journal of Japanese Studies* 422.

28 Joseph Davis (1996), *Dispute Resolution in Japan,* p. 139–141; N.Kashiwagi (1992), *'Nihon no torihiki to keiyaku hō'* (Japanese Trade and Contract Law), 500 New Business Law 22–23. In Japan, as in other modern industrialised countries, it is especially in the termination stage of the continuing commercial contract that law might matter. The desire to terminate can often provide the impetus for driving dispute resolution into the formal legal arena. At this stage, the parties may not shy away from legal action because they accept that the commercial relationship will collapse.

suggested retail price systems, the dispatch personnel system and returns to manufacturers of retailers' unsold products.[32]

### 3.2
### Common Types of Unilateral Termination by Manufacturers

According to Japanese legal practitioners the following two types of termination occurred regularly in the 1990s.[33] One type of termination occurs when manufacturers wish to cut costs. In these cases the manufacturer finds a better alternative or takes distribution into its own hands, thereby expending with the services of the distributor. This usually happens after the distributor has expanded the sales of the manufacturer's products and the market has reached saturation point. Since many distributors in Japan are very inefficient, which causes high retail prices, this type of termination has always occurred frequently, and can be considered to be a natural process.[34] However, recently this type of termination has undoubtedly increased when the pressures to lower prices have become so much stronger.[35]

One other common type of termination relates much more to the current pressures upon the Japanese distribution system. This type of termination occurs when leading manufacturers cancel contracts with distributors who sell the products at prices which are lower than those agreed upon with the manufacturer. These terminations have been brought about by the rise of regular distributors which turned themselves into discounters starting in the 1990s. It concerns distributors who want to increase their competitive power and expand their sales by lowering resale prices. This second type of termination frequently occurs in industries where leading manufacturers enjoy a great deal of control over the majority of their distributors.[36] They want to keep resale prices at a certain level and decide to terminate the contract. Furthermore, they might have been subject to pressure from regular distributors which are forced to compete with such discounters.

## 4
## PROBLEMS FOR DISTRIBUTORS AND THE LEGAL RESPONSE

Distributors sometimes take legal measures after a termination of the contract because terminations can be very damaging to them. Manufacturers can cause a great amount of

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29 See M.Sugawara and S.Saito (1998), *'Furanchaizu hikari to yami'* (Franchise, Light and Darkness) in: *Nikkei Business* 23 February 1998, p. 23–24; Also H.Tanaka and K.Fukazawa (1998) 'Furanchaizu *no jigoku*' (The Franchise Hell) in: *Shūkan Daiyamondo* 20 June 1998, p. 24–45.

30 See on the increasing dependence on civil remedies before the civil courts during this period of deregulation: Kenji Kawagoe, Hiroshi Takahashi, Yoshihisa Nōmi, Kazuhiko Bandō (1998), *'Kisei kanwa jidai ni okeru hō no jitsugen'* (Law Enforcement in a Period of Deregulation), 632 *New Business Law* 4–16; 633 *New Business Law* 43–51. *(Zadankai)* (Round Table Discussion).

31 Nihon Keizai Shinbun (ed.) (1993), *Ryūtsū gendaishi* (Modern History of Distribution), p. 358–359. The factors which I have referred to are by no means exhaustive. But an overall overview of all the relevant factors falls beyond the scope of this study. For example, the strong growth of large-scale retailers can also be regarded as influential. See Roy Larke (1994), *Japanese Retailing*.

damage to a distributor if they cancel a distribution agreement. A distributor may be very dependent on the continuation of the contract and may also be vulnerable to the unscrupulous behaviour of the manufacturer, having invested in equipment or specialised knowledge to fulfil the contract. The longer the relationship has lasted the more dependent a distributor might have become. In most cases the distributor does not merely resell the product of the manufacturer, but also provides sales promotion and after sales service in which it has heavily invested. In addition, frequently the distributor's business is for a great deal dependent upon one single product line.[37] It may therefore be difficult for the distributor to use its existing infrastructure to substitute one product line for another.

Generally speaking, the Japanese distributors can be very dependent on manufacturers, which is caused by the strong interference of manufacturers in their affairs. This interference is usually made effective by various sorts of financial assistance to the distributors.[38]

## 4.1 Contract Law

Distributors have increasingly invoked the principle of good faith in order to claim compensation or specific performance of a contract, arguing that the termination was invalid. However, this leads to one core problem in contract law. On the one hand, there is the principle of freedom of contract which implies the freedom to terminate a contract at will. A manufacturer must control the quality of the product and the services offered by the distributor in order to ensure the trademark's resale value and to increase sales. If the manufacturer is discontent with the performance of the distributor, it is not obliged to remain with its distributor for eternity.

On the other hand, there is the principle of good faith which sets limits on the freedom of contract. The weaker party must be safeguarded from the manufacturer's opportunism. It follows that in the contractual law governing the unilateral termination of the distribution agreement there is a tension between the competing principles of the freedom of contract and the protection of reasonable expectation as embodied in the good faith principle.

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32 See also the report of January 1998 from the Manufactured Imports Promotion Organisation (MIPRO) entitled: *Distribution System and Business Practices in Japan—Changes and Prospects,* p.7–10.

33 N.Kashiwagi, K.Kawagoe, K.Iwaki and K.Shindō (1995), o. c., p. 7–9.

34 N.Kashiwagi, Ibid.

35 Ibid.

36 These systems are often referred to by the Japanese term *'Distribution keiretsu'* describing the organisation and control of channels by a particular manufacturer in which the wholesale and resale outlets become integrated by means of a variety of ties and links. However, these kinds of distribution systems are also common in many other industrialised countries.

### 4.2
### Anti-trust Law

In an increasing number of cases Japanese anti-trust law has a strong indirect influence on termination disputes. Stricter enforcement of the Anti-monopoly Act has resulted in more distributors invoking the Act after distribution agreements have been cancelled or supplies have been stopped. This concerns the second type of termination which occurs when manufacturers allegedly only cancel the agreement because the distributor sells at prices lower than those agreed upon with the manufacturer. This constitutes resale price maintenance which is in violation of the Act.

Recently, in a number of industries such as within the distribution system for luxury cosmetics, mobile phones,[39] computer game software,[40] and designer sports shoes,[41] distributors have filed complaints with the Fair Trade Commission (FTC), the agency which enforces the Act, for an alleged breach of this Act after terminations of the contracts or threats to do so. It is important to note that not only the termination itself but also the clauses on which this is justified may violate the Act. Manufacturers sometimes cancel contracts with distributors because they do not abide by their trade policies which are laid down in their contracts. When these trade policies themselves are in violation of anti-trust law, the termination may be illegal.[42]

Therefore, in some cases, in addition to invoking contract law the Act has been invoked before the civil courts in order to deny the validity of the termination. This has been done by distributors of luxury cosmetics and jeans. Finally, it must be noted that in contrast to laws such as the Civil Code, which focus their attention on circumstances at a micro-level, the Anti-monopoly Act primarily focuses on macro-level conditions. More than on the parties themselves, the Act focuses on the market, making it very distinct from other laws.

## 5
## THE MAIN PURPOSES OF THIS STUDY

The first purpose of this dissertation is to investigate the role of Japanese law in protecting the distributor against unilateral terminations of distribution agreements, and to gain an insight into how this law has developed in recent years. This is not limited to a study of so-called 'black-letter' law (case law and legislation) but also involves a sociological study of the application of law in actual practice. A study of only black-letter law would not tell us very much about the sociology of law in Japan.

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37 T.Ōta (1998), *Gendai kigyō torihikihō* (Contemporary Trade Law of Corporations), p. 195.

38 See Kenji Sanekata (1994), *Ryūtsū torihiki kankō shishin no jikkōsei—Nihon shijō no heisasei tokushusei ni taisuru inpakuto* (The Effectiveness of the Guidelines concerning Distribution Systems and Business Practices—The Impact on the Peculiarity and Closed Nature of the Japanese Market), in: Keizai Hōgakkai (ed), *Nihon no torihiki kankō to dokkinhō* (The Japanese Trade Practices and the Anti-monopoly Act), p. 3.

My first interest concerns the way in which Japanese contract law deals with the tension between the principles of good faith (protection of the weaker party) and the freedom of contract.

Secondly, I am interested in the increasingly important role of anti-trust law when terminations of distribution agreements occur. This involves, in the first place, research into terminations of distribution agreements that may constitute a breach of the Anti-monopoly Act. This is difficult to establish since the manufacturer will rarely explicitly state that it has terminated because the distributor has violated a duty such as resale price maintenance which in itself violates the Act.

If a violation is acknowledged, the second question is whether the termination, or the clause justifying it, is void. This depends on the way the court responds to the general question of the enforceability of contracts in violation of the Anti-monopoly Act. This requires an investigation into the subtle relationship between contract law and anti-trust law, which may both be applicable. This is a topic which is gaining much interest among Japanese legal scholars. Competition might exist between the decisions of the FTC and the civil courts. In order to understand the peculiarities of the way in which Japanese jurisdiction deals with these issues I will present an overview of the response by Dutch law to similar problems caused by terminations of distribution agreements for 'illustrative' purposes.

The second purpose of this study is to use the findings of my field research in Japan and the comparison with Dutch law in order to contribute to some extent to the lively academic discussion about whether or not there are distinct Japanese attitudes toward contracts, and if so whether they are mainly due to cultural factors or not. This kind of research is not only interesting from a purely theoretical point of view but also from a practical viewpoint. Japan's influence on the global economy as the second largest economy in the world is enormous and the number of foreign companies, which establish contact with Japanese distributors, is increasing. For this reason the number of contracts concluded with Japanese companies where Japanese law is chosen has gradually increased.[43] In international dealings termination disputes between manufacturers and distributors are very common.[44] Foreign companies regularly terminate contracts with distributors in Japan which requires some understanding of the legal implications this might have.[45]

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39 This generated an FTC Recommendation against three manufacturers of mobile phones on 18 November 1997.

40 See *Nikkei Weekly*, 26 January 1998.

41 See *Nikkei Weekly*, 1 December 1997. This generated an FTC Recommendation against Nike Japan Corporation on July 28, 1998.

42 For example, it is expected that in an increasing number of cases the issue will be whether contract clauses within distribution, franchise and technical licence agreements are in violation of the Antimonopoly Act. See Hiroshi Iyori (1999), *'Keshōhin taimen hanbai jōkō ni kansuru saikōsai no futatsu no hanketsu'* (Both Supreme Court Decisions in relation to the Cosmetics Face-to-face Sales Clauses) 658 *New Business Law* 11–15.

Generally speaking, more knowledge of Japanese law as it actually operates and Japanese contract attitudes can provide a great deal of new information for Western companies doing business with the Japanese. Practitioners' views and some preliminary research suggest that Japanese contracting practices in international markets not only adjust to, but also contribute to the development of international norms.[46]

## 6
## STRUCTURE OF THIS STUDY

First, applicable Japanese contract law and anti-trust substantive law will be investigated in detail. This includes a study of legislation, case law and legal doctrine with a brief analysis of its historical development.

Second, in order to gain an insight into this Japanese law an approach along the lines of the sociology of law is important.[47] Generally speaking, a study of the mere black-letter law of a country does not provide much information about law in action, since this may differ considerably. The political, economic and cultural context of the applicable law also needs to be studied.[48]

This first requires a study of the access to the civil courts and the FTC and any possible barriers which may exist. In order to investigate how distributors can be protected not only substantive law but also procedural matters are studied.

Second, this requires a study of people's attitudes to law and for this reason I conducted a few case studies, involving a detailed analysis of some legal termination disputes between manufacturers and distributors. I first present a description of the chronological development of these disputes, followed by an evaluation and (tentative) conclusions. The insights gained in such a way add significantly to our understanding of Japanese law, insights that cannot be derived from assumptions about Japanese law in general. My main purpose has been to gain an insight into the motives for the actions of the principal actors involved in these disputes.

Other methods of sociological research into the role of law in Japan such as sending questionnaires to companies and individuals have been frequently carried out, but detailed case studies are still few in number. They might therefore be considered a supplement to the sociological research which has already been carried out mostly by the Japanese themselves. The presentation of such case studies also serves to reveal a rarely discussed

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43 Hiroshi Oda (1992), *Japanese Law,* p. 12

44 K.Egashira (1992), o. c., p. 209.

45 In a recent symposium held in Japan between European and Japanese legal scholars and practitioners a great deal of attention was directed towards the termination disputes between European and Japanese companies. See EU-Japan Legal Dialogue: Contract, (Kyoto, November 21–22, 1996). The papers presented during this symposium can be found on the Internet site: http://www.kclc.or.jp/EUdialogue/EU.htm.

46 V.Taylor (1993), o. c., p. 370.

side of Japanese business practice, namely the termination of a continuing commercial contract. I have decided to limit myself to case studies in one particular industry. I have chosen to describe some termination disputes within the Japanese distribution system for luxury cosmetics.

## 6.1
## Case Studies within the Luxury Cosmetics Industry

Particularly within the distribution system for luxury cosmetics there have been a number of famous legal termination disputes which started at the end of the 1980s, most of which have ended only recently. These disputes are also directly related to the recent pressures on Japanese distribution systems to restructure and lower prices. In these disputes not only contract law but also anti-trust law play an important role and distributors used all possible legal remedies to the bitter end, without compromise. These disputes have therefore generated many influential decisions on the part of the higher courts and the FTC. Accordingly, they can provide an insight into the various ways in which Japanese law may protect the distributor in practice. They also clarify the subtle interplay between contract law and anti-trust law. Finally, it must be noted that these disputes exerted much influence upon the luxury cosmetics industry and other comparable industries.

My mode of operation for these in-depth case studies is explained in much detail in chapter 4. I have collected various kinds of primary material such as formal court decisions and standard-form contracts. In addition, I conducted numerous interviews during two periods of field research in Japan. The first interview sessions were held during the second half of 1994. The second interview sessions were held during the month of November 1997. These interviews were conducted in Japanese with the principal actors to these disputes such as the parties themselves, their lawyers, a Tokyo High Court judge who had rendered a very influential decision in these cases and an FTC official.

I conducted open semi-structured interviews in which I focused on the facts without enquiring about their opinions. Based on a chronological list of facts, as I understood them from court decisions and articles in Japanese newspapers, I asked them to give me their version of the facts and to explain the motives for their actions. In addition, I carried out interviews with third-party observers such as a journalist, an editor of a magazine on the cosmetics industry and a MITI bureaucrat with a great deal of information about this industry. They could provide facts which I had not been able to collect myself. Finally, I gathered much secondary material such as articles in newspapers, magazines and books about these cases.

I have not described all the litigated termination disputes within the luxury cosmetics industry, only the most influential ones. These are limited to the Tokyo region which

47 See K.Kawagoe (1988), o. c., p. 1.

48 Annette Marfolding (1997), 'The Fallacy of the Classification of Legal Systems: Japan Examined', in: V.Taylor (ed.), *Asian Laws Through Australian Eyes,* p. 47.

generated the largest number of formal decisions by the civil courts and the FTC. My findings can, however, provide insights into the possibilities for distributors in the cosmetics industry to use legal measures to fight against the unilateral termination of the distribution agreement. They provide an insight into the role of contracts and contract law and the influence of the Anti-monopoly Act.

## 6.2 Comparative Approach

I have also taken a comparative approach. My comparison with the legal response in one other European country is, however, only used for 'illustrative' purposes. Choosing one country also functions to escape from a 'West vs. Japan' type of mental framework. Such an approach tends to generalise in vague cultural terms, without clearly defining causal links.

Unilateral cancellations of distribution agreements by manufacturers are a phenomenon which is common to many industrialised countries and the solutions provided by Japanese law can therefore serve as an interesting reflection of judicial intervention in contract law when comparing them to the solutions in another comparable modern industrialised country. This might be fruitful when the Japanese findings are compared with the legal response of a modern industrialised country which faces similar problems and which has a comparable legal system. Furthermore, a study of termination disputes within a comparable distribution system of luxury cosmetics as in Japan may provide new insights.

The first purpose is to put the results of my research on the termination of distribution agreements in Japan into perspective in order to obtain a better understanding. This requires not only a comparison of black-letter law but also of political, economic and cultural factors. This comparison also has a sociological dimension, because I compare the practices of manufacturers and distributors in responding to their national laws.

I must emphasise that I will not conduct a comparative law study in the true sense of the term. The purpose of the comparison is not to find useful answers for similar problems in Japan or to aim at some sort of convergence. The comparison is for illustrative purposes only.

I do not focus on comparative law theories as I believe that any classification of Japanese law in a 'legal family', which has been an important technique for comparative law scholars to enhance the understanding of foreign legal systems, is likely to lead to misconceptions rather than an understanding of the system. A classification of the Japanese legal system as part of the 'civil law' family does hardly contribute to an understanding of Japanese law. The Japanese legal system, as indeed do other systems, needs to be understood in its own cultural, economic and political context. Even if black-letter law as expressed in legislation and caselaw may turn out to be quite similar, the political and cultural context of law, such as the provision of access to dispute resolution fora and people's attitudes to law, may lead to a divergence rather than a convergence of actual living law. For an assessment of actual living law in Japan cross-disciplinary analysis is indispensable.[49]

In order to put my Japanese findings into perspective I have chosen to compare them with Dutch law.

## 6.3
## Dutch Law and Practice as a 'Comparative Illustration'

The reasons for choosing Dutch law for my comparison are as follows: First, there exist some similarities between Japan and the Netherlands. In the Netherlands, where distribution plays an important role in the economy similar problems may arise as in Japan when a manufacturer terminates a distribution agreement. Furthermore, the Dutch legal response to these problems shows many similarities with the Japanese response. In each of these countries there is no direct legislative response for the protection of the interests of the distributor and judicial intervention has been the main source of law.

Another similarity is that over the years Dutch contract law has also been strongly influenced by subsequently French, German and Anglo-American law. Another important resemblance is to be found in the increasing role of anti-trust law. In 1998 a new Dutch Competition Act was enacted and, as in Japan, this has been done partly because of outside pressure (from the EU Commission). Because of the new Act, which is more in line with EU anti-trust law, increasing importance is being attached to the inter-relationship between private law and anti-trust law. This also has an influence on termination disputes involving distribution agreements.

Finally, in my opinion a comparison with the Dutch approach may be very rewarding since there are some similarities in legal culture between the Netherlands and Japan. For example, the Netherlands is also a litigation-avoiding culture. Comparisons in a wider international context show that only the Japanese handle their conflicts with less litigation. This corresponds with the comparatively low numbers of advocates and the judiciary in both countries.[50]

Second, there are also practical reasons for choosing Dutch law. I grew up in the Netherlands and I obtained a major at M. A. level in Dutch law. Furthermore, I have had two and a half years' experience as a part-time employee in one of the largest Dutch law firms, Trenité van Doorne, where I had many opportunities to gather first-hand information about the applicable Dutch law on the termination of distribution agreements.

A third reason is that both countries have strong business relationships and termination disputes involving distribution agreements concluded between Dutch and Japanese parties

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49 See A.Marfolding (1997), Ibid., p. 1–48. Marfolding demonstrates this thesis by comparing dispute resolution and civil procedure in Japan with that in Germany. Although large-scale reception of German laws and German legal theory has led to many similarities in black-letter law, she demonstrated that there are substantial differences in the law in action. See also Volkmar Gessner (1995), 'Presumptio Similitudinis? A Critique of Comparative Law', in: Proceedings of the 1995 Annual Meeting of the Research Committee on Sociology of Law (International Sociological Association), Legal Culture: Encounters and Transformations (Tokyo, August 1–4, 1995); See also O.Kahn-Freund (1974), 'Uses and Misuses of Comparative Law', 37 *Modern Law Review* 1–21; Finally, see Luke R. Nottage (1997), 'Contract law and Practice in Japan: An Antipodean Perspective', in: H.Baum (ed.), *Japan: Economic Success and Legal System,* p. 213. He agrees with Marfolding that traditional analytical distinctions are too abstract and comparative law studies encompassing Japan will need to become more ambitious in exploring cultural, political and economic realities.

also occur frequently. During my work at the Dutch law firm, on a number of occasions I was faced with dealing with problems, which had been caused by a Dutch party which had terminated a distribution agreement with a Japanese distributor in Japan. Furthermore, since many Japanese companies do business in the Netherlands,[51] terminations of distribution agreements by Japanese manufacturers with Dutch distributors are also likely to occur frequently.[52]

The model of analysis of Dutch law as an illustrative comparison is similar to the model used in Japan. It involves a study of case law, legislation and legal doctrine. In addition, procedural matters are investigated such as the ease of access to the formal dispute resolution fora. Moreover, I also conducted brief empirical research into termination disputes within the distribution system for luxury cosmetics which is comparable to the system in Japan. In addition to analysing the few litigated termination disputes in this industry which have led to court decisions, I gathered further information with a collection of standard-form contracts and interviews with several Dutch lawyers and businesspersons involved in termination disputes within this industry.

As pointed out above, my definition of distributorships may be applied both to Japanese and Dutch distributorships, due to a number of common characteristics. Neither Japanese nor Dutch law provide legal definitions of distribution agreements.[53]

I concede that in actual practice distribution agreements within the Netherlands may differ to some extent from those used in Japan. However, the consequences resulting from the unilateral termination of these agreements are very similar.

## 7
## DISCUSSION ON JAPANESE ATTITUDES TOWARD CONTRACTS

As referred to above, the second purpose of this book is to participate in the discussion among many Japanese and non-Japanese scholars about Japanese attitudes toward contracts.

In order to obtain a better understanding of this discussion it is important to refer briefly to the fact that the Japanese Civil Code and Commercial Codes were adopted at the end of the 19th century largely along the lines of the German Civil and Commercial Codes. In a very rapid fashion the Japanese government had adopted Western European law including these two Codes, because it hoped that the introduction of a legal system along 'Western lines' would facilitate the revision of the 'unequal treaties' with the Western nations in

50 Erhard Blankenburg and Freek Bruinsma (1994), *Dutch Legal Culture,* p. 4.

51 During the first three quarters of 1998 the Netherlands had the third largest share, of any EU country, of imports from Japan (12%). See Dujat Newsletter, April 1999.

52 For example, one indication is a recent JCC (Japanese Chamber of Commerce) seminar,' Agency and Distribution Agreements and the new Dutch Competition Act' organised by the largest Dutch law firm Nauta Dutilh on 18 March 1998 which was attended by many Japanese businessmen stationed in the Netherlands. Many questions dealt with termination matters.

which the principle of extra-territoriality[54] was established. Furthermore, it wanted to turn Japan into a strong country which necessitated the establishment of a centralised political system and uniform legislation as one of its bases.

It is of great importance to note that these Codes were established by government guidance. Therefore, this might have resulted in a large gap between law in the books and actual practice. The lawmakers construed Western law in traditional East Asian terms: law as an instrument of the pervasive administrative state. Only gradually did they adjust to the underlying premises of private law in a liberal political order.[55]

Accordingly, the reception of this foreign law triggered strong interest among Japanese scholars in how this law, with principles such as private autonomy and the binding power of contract, became internalised within Japanese society.

The lively discussion on Japanese attitudes toward contracts started in the 1960s with a famous work by the legal sociologist Takeyoshi Kawashima.[56] He and many other scholars after him focused strongly on the dualism between adopted foreign contract law and Japanese commercial practice, explaining this by cultural factors. In this approach it is thought that law is largely irrelevant for the Japanese. Instead, the business relationship is most important. Furthermore, in their view the Japanese favour unwritten or very brief contracts. They do not regard themselves as being bound by the letter of such agreements but rely on the flexible attitude of the other party to seek renegotiation. If a dispute arises they will rarely allow the matter to proceed to court.

Most earlier studies were sweeping comparisons with the West, especially between Japan and the US, emphasising that distinctive features in the two systems could be attributed to a different consciousness as regards the contract. In this approach much emphasis was placed on the Japanese uniqueness. These legal scholars argued that the Japanese view of contract was somehow linked to the genesis of Japanese society.

However, over the years more and more legal scholars started to raise doubts about the existence of distinctive Japanese contracting practices and a typical Japanese concept of contract. Even if they recognised distinctive Japanese features, they no longer explained them as being due to cultural factors. Less emphasis was placed on the uniqueness of the Japanese situation. In their opinion, sweeping comparisons with the West had outlived their use and they preferred more detailed empirical studies.

On the basis of my own research into one aspect of the contractual relationship, namely the termination of distribution agreements, I hope to be able to contribute to this discussion and to provide comments on what some legal sociologists have said about Japanese attitudes

53 For a somewhat comparable definition see: J.M.Barendrecht and G.R.B.van Peursem (1997), *Distributieovereenkomsten* (Distribution Agreements), p. 3; See also C.A.M.van de Paverd (1999), *De Opzegging van Distributieovereenkomsten* (The Termination of Distribution Agreements), (PhD Thesis Amsterdam), p. 13.

54 This meant that foreigners were allowed to use their own consular courts and laws. The Japanese government believed that treaty revision could only be achieved if the same kind of political, legal and economic system as that of the Western nations was adopted.

toward contracts. It must further be noted that within this discussion much attention has been directed towards the role of contracts and contract law in continuing trade relations between Japanese companies. Many Japanese have studied Japanese domestic commercial trading relationships in order to reach conclusions about Japanese attitudes toward contracts. Therefore, my own analysis of distribution agreements as one type of commercial contract might enable me to make a contribution to this discussion.

## 8 EXPLANATION OF THE FOLLOWING CHAPTERS

My research is structured as follows. In chapter 2 substantive Japanese contract law will be described with a brief historical analysis and a reference to the ease of access to the civil courts. The largest part will be covered by Japanese case law and legal literature. In chapter 3 I will describe and analyse Japanese substantive anti-trust law with much focus on the private law enforcement of the Antimonopoly Act. Chapter 4 will be the most important chapter in which the case studies are presented in much detail. The findings of this chapter will for the greater part contribute to my conclusions. Chapter 5 highlights the applicable Dutch substantive law for illustrative purposes. In addition I have carried out some empirical research into the law in practice in the Dutch distribution system for luxury cosmetics in order to put my field research in Japan into a more appropriate perspective. In chapter 6 I will present the still continuing discussion concerning Japanese attitudes toward contracts with some of the most important contributors to this discussion. In the same chapter I will draw some conclusions and hope to contribute to some extent to this discussion. Although I have focused only on the termination phase of the continuing contract, the results show that this allows us to draw a number of interesting conclusions.

55 J.O.Haley (1991), *Authority Without Power—Law and the Japanese Paradox,* p. 72.

56 Takeyoshi Kawashima (1967), *Nihonjin no hō ishiki* (The Legal Consciousness of the Japanese). Partially translated by Charles S.Stevens as 'Contract Consciousness of the Japanese' (1974), *Law in Japan,* Vol. 7, p. 1–21.

# 2
# Japanese Contract Law and the Unilateral Termination of Distribution Agreements

## 1
## INTRODUCTION

When manufacturers/suppliers terminate distribution agreements, distributors may incur serious losses. The distributor has to leave the distribution network and sever its links not only with the supplier but also with its own customers which are loyal to the product. It may have relied strongly on the continuation of the contract, having invested heavily in the continuing trade relationship. Japanese distributors are usually small or medium sized companies and may be very dependent on the continuation of supplies. Frequently, the distributor's business is for a great deal dependent upon one single product line.

The interests at stake can be such that the distributor may readily engage in a bitter dispute in order to try to limit as far as possible the damaging consequences. Some distributors have taken legal steps in order to receive compensation or to secure the supplies.

In the 1990s these kinds of termination disputes have increased in number. Pressures to cancel continuing contracts unilaterally have increased. The period of stagnant economic growth during the 1990s and significant pressures both to lower prices and to restructure companies have placed a greater strain on many historically stable continuing contracts. Large manufacturers have cut back on distributors and therefore have stopped providing goods to them. With litigation as their only recourse, these distributors do sometimes rather risk litigation than to settle. In these cases the distributors have often claimed damages and have sometimes demanded specific performance.[1]

The central theme in this chapter is to investigate the role of contract law in Japan as a means of protecting the distributor against unilateral terminations of distribution agreements. Distributors may invoke general principles of contract law in which there is a tension between the competing principles of the freedom of contract and the protection of the weaker party or the justified expectations toward the continuation of the contract.

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1 See Joseph Davis (1996), *Dispute Resolution in Japan,* p. 139–141.

# 2
# JAPANESE CIVIL AND COMMERCIAL CODES

## 2.1
## Introduction

There are no specific provisions in the Japanese Codes governing distribution agreements. Because these agreements are a type of sales agreement they are governed by general Japanese contract law. As in other civil law systems, such as the Dutch system, party autonomy is the core concept within Japanese contract law. This is reflected in the Japanese Civil and Commercial Codes which were both adopted at the end of the 19th century, based largely on the German Civil and Commercial Code.[2] They do not prescribe the form that contracts must take in order to be valid. Many non-compulsory provisions only state general rules which may be varied and departed from by the parties. Distribution agreements, however, do not fall under the many specified contracts in either Code.[3] Furthermore, principles of contract enshrined in the Japanese Civil Code generally presuppose short-term contractual relationships.[4] For example, the general provisions on contract allow termination as of right. Article 541 states that:

> If one of the parties does not perform his obligation, the other party may fix a reasonable period and demand its performance, and may rescind the contract, if no performance is effected within such period.[5]

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2 The Civil Code was enacted in 1898 and the Commercial Code in 1899. Much has been written about the complications involved in the introduction of both Codes. See for many sources Meryll Dean (1997), *Japanese Legal System: Text and Materials,* p. 72–74.; J.O.Haley (1991), *Authority Without Power—Law and the Japanese Paradox,* p. 75–77. The centenary of the Civil Code has been commemorated with several symposia and books and articles. See, for example, the special feature in the legal journal *Juristo* Vol. 1126 (1–15 January 1998), entitled: *Minpō hyaku nen—shinjidai no minpō o tenbō suru* (A Hundred Years of the Civil Code—Prospect of Civil Law in the Coming Age); and a four-volume set entitled: *Minpō no hyaku nen* (A Hundred Years of the Civil Code), Toshio Hironaka and Eiichi Hoshino (eds.).

3 Chapter 2 of Book 3 of the Japanese Civil Code provides rules for several typical types of contracts such as sales contracts and exchanges. Chapters 2 to 10 of Book 3 of the Commercial Code provide rules for specific commercial contracts such as sales between merchants, transport contracts etc.

4 See Veronica Taylor (1993), 'Continuing Transactions and Persistent Myths: Contracts in Contemporary Japan', 19 *Melbourne University Law Review* 379.

5 Translation in EHS Law Bulletin Series, published in Tokyo by Eibun Hōreisha (hereafter EHS Translation), p. 90.

6 See V.Taylor (1993), o. c., p. 379–383.

7 For leases see Civil Code Arts. 601–22, for employment Arts. 632–31.

Although some legal scholars argue that this creates the right to terminate a continuing contract at will, a breach of contractual obligations which are not essential for the continuation of the distribution relationship will usually not justify a unilateral termination based on Article 541.[6]

Exceptions to the rule that the Civil Code generally presupposes short-term contracts are the provisions dealing with leases *(chin taishaku)* and employment *(koyō)*.[7] Since some of the provisions stipulated that these contracts are terminable at any time, they did cause problems for tenants and employees.[8] Therefore, they were amended by judicial and statutory intervention which favoured the preservation of the transaction in order to protect the weaker party. They were eventually replaced by special statutes on labour law such as the Employment Standards Law *(Rōdō kijun hō)* and the Land and House Lease Law *(Shakuchi shakka hō)*. They strongly favour the continuation of these contracts after the expiration of the contract term.[9] It is unclear whether the original Civil Code provisions can now be applied by analogy to new kinds of continuing contracts such as distribution agreements.[10]

## 2.2 Article 1 of the Japanese Civil Code

In relation to the termination of distributorship agreements the general clauses of the Civil Code are of very great importance. In the compulsory provision of Article 1 of the Civil Code in sections 2 and 3 the concepts of good faith and abuse of rights are stipulated. The article reads:

> 1) All private rights shall conform to the public welfare.[11]
> 2) The exercise of rights and performance of duties shall be done in faith and in accordance with the principles of trust.
> 3) No abusing of rights is permissible.[12]

This article was incorporated into the Civil Code in 1947 during the implementation of post-war legal reforms. The Japanese courts have extensively applied sections 2 and 3 when distributorships have been unilaterally terminated. Most such decisions have appeared since the 1960s.[13] Before the incorporation of Article 1 in the Civil Code, there had also been judicial precedents in which the principle of good faith was applied. This was done in order to soften the negative effects of a strict application of classical contract law. However, in the judicial precedents from the 1920s until the 1960s the principle of good faith was mostly applied in order to restrict the cancellation of a lease contract but not a distribution agreement.[14]

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8 For leases see Article 617, for employment see Article 627.

9 For the Land and House Lease Law which was enacted in 1992, see Articles 3–9 on land lease and Articles 26–30 on house lease. Article 28 requires serious reasons for any valid cancellation. See for the Labour Standards Law enacted in 1947 Articles 19–21. As will be explained later in this chapter-these articles may be abolished in the near future.

## 2.3 Custom

It is important to note that custom *(kanshū),* which may be very important in commercial transactions, has been formally recognised in both Codes as a source of law. Although Article 1 of the Commercial Code allows reference to custom only in the absence of code provisions,[15] Article 92 of the Civil Code places a completely different emphasis on custom. It reads:

> If in cases where there exists a custom which differs from any provisions of laws or ordinances which are not concerned with public policy, it is to be considered that the parties to a juristic act have intended to conform to such custom, that custom shall prevail. (EHS Translation, p. 17).

This means that in certain situations custom can be an important source of law. As in other civil law countries such as the Netherlands it has an important function in order to fill the gaps between formal law and social reality.[16] For example, some traditional transaction practices in the Japanese distribution system such as consignment sales *(itaku hanbai)* are not specifically mentioned in written law. Nevertheless, as in other areas of commercial law, widely accepted commercial practices that are not in conflict with written law are likely to produce legal obligations that a court may be asked to uphold, as is the case with other parts of customary law. Actual practice shows that Japanese courts have frequently treated customary law in this way.

In one case the court held a twenty-year contract for the wholesale distribution of magazines and textbooks unenforceable, in part because contracts of such long duration were not customary in the wholesale book trade.[17]

## 2.4 Provisions on Commercial Agency Agreements

Finally, some reference must be made to the provisions on the termination of commercial agency agreements *(dairishō keiyaku),* which share some similarities with distribution agreements. Article 50 (1) of the Commercial Code stipulates that a commercial agency agreement with no fixed period can be terminated by giving two months' notice. However, this provision is optional and does not have much practical significance. It is usually not

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10 See V.Taylor (1993), o. c., p. 379.

11 Section 1 does not have much practical relevance in Japan. See Guntram Rahn (1990), *Rechtsdenken und Rechtsauffassung in Japan,* p. 177–180.

12 EHS Translation, p. 1.

13 Takashi Uchida (1993), *'Gendai keiyakuhō no arata na tenkai to ippan jōkō'* (General Clauses and New Developments in Contemporary Contract Law), 516 *New Business Law* 22–24.

14 Ibid.

applied by analogy to the termination of distribution agreements.[18] This lack of regulation can be contrasted with the situation in many Western European countries such as the Netherlands where there are detailed compulsory provisions concerning commercial agency agreements, including their termination.[19]

The concept of agency in Japan does not differ substantially from that of other jurisdictions and agents might be confronted with similar problems as distributors after termination.

However, generally speaking the amount invested by commercial agents in Japan is usually lower than the amount invested by distributors. This reduces the need for legal protection in cases of unilateral termination of these contracts.[20] Therefore, Japanese courts and legal scholars often hold that commercial agents stand independently of the companies with which they transact and contracts may be terminated as of right, with no ancillary obligation to compensate for any resulting loss.[21]

## 3
## CASE LAW

### 3.1
### Introduction

It is important to focus on Japanese case law since it is mainly in judicial decisionmaking, which has shown much creativity, that distributors have found some protection against unilateral terminations of distribution agreements.

Since the 1980s a number of Japanese practitioners and legal scholars started to analyse all the reported court decisions concerning termination disputes relating to continuing commercial contracts. Their intention was to try to find some guidelines which could be taken from case law.[22] A Japanese legal scholar, Hiroyasu Nakata, analysed 114 decisions involving the termination of continuing commercial contracts, covering the period from the start of the 20th century until 1994. In 90 cases the dispute was triggered by a unilateral termination of a distribution agreement. On 64 occasions the manufacturer/supplier cancelled the distribution agreements with the distributor.[23] In most of these cases the distributors claimed damages from the manufacturer, contending that the suspension of supplies and the cancellation of the contract were illegal.

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15 Article 1 of the Commercial Code reads: 'As to a commercial matter, the commercial customary law shall apply if there are no provisions in this Code; and the Civil Code shall apply if there is no such law'. (EHS translation, p. 1).

16 See on the importance of custom in Japan, V.Taylor (1993), o. c., p. 364–370; also M.Dean (1997), o. c.,p. 152–153.

17 See *Asahi Shoseki Hanbai K.K.v.Suzuki Takashi and Saijō Kanji,* 1045 *Hanrei Jihō* 105 (Tokyo District Court, 30 September 1982).

18 See Kenji Kawagoe (1988), *'Keizokuteki torihiki keiyaku no shūryō'* (The Termination of Continuing Trade Contracts) 18 *New Business Law (Bekkan)* (Separate Volume) p. 10.

Sometimes, particularly when the products on order were special brands with a distinctive character which could not be obtained elsewhere, the distributors demanded specific performance instead of damages. In these cases the distributors desperately wanted these supplies in order to prevent losing their customers.[24] This demand for specific performance mostly took place by means of a provisional disposition *(karishobun)* procedure where a distributor applied for a disposition temporarily determining the state of affairs with respect to the legal relationship in dispute. In these cases distributors sought confirmation by the court that the contract was still valid. To secure the supplies which had been on order they also demanded an injunction for the delivery of those goods. Only in a few cases did the distributors demand legal confirmation of contractual rights and the supply of deliveries in a main civil suit.

When the courts have been asked to intervene in termination disputes involving a distribution agreement the reason for litigation is often the absence of any specific rules governing this type of transaction and deliberately vague party choices.[25] So far, most of these disputes have concerned distribution relationships in which no written contracts were concluded. Recently, though, in more of these disputes the parties in question had concluded contracts in writing.[26] Usually these termination disputes involved medium and small sized companies. This is because they often terminate contracts in a more abrupt manner than larger companies which leaves the other party with no option but to litigate.[27] When deciding on unilateral terminations of distributorship contracts, the courts usually call such contracts 'continuing supply contracts' *(keizokuteki kyōkyū keiyaku)* or 'continuing trade contracts' *(keizokuteki torihiki keiyaku).*[28] The applicable Japanese case law is primarily determined by lower court decisions.

It must be noted, however, that termination disputes, which lead to litigation and final judgement, are rare. The cases that I will describe are only the tip of the iceberg of the

19 Although in the Netherlands these provisions cannot be interpreted by analogy they still function as an important reference. K.Kawagoe compared Japan and Germany in this respect and attributed the lack of regulation in Japan to the fact that commercial agencies do not play such an important role within distribution as they do in Germany. See K.Kawagoe, Ibid., p. 12.

20 See Yasuzo Takeno (1997), in: Agustin Jausas (ed), *International Encyclopedia of Agency & Distribution Agreements,* p. 3; and Keiji Matsumoto (1996), in: Richard Christou (ed), *International Agency Distribution and Licensing Agreements,* p. 489.

21 V.Taylor (1993), o. c., p. 381; See *Konō v. Yasuda Kasai Kaijō Hoken K.K.,* 327 *Hanrei Taimuzu* 314 (Yokohama District Court, 28 May 1975).

22 For example, in 1988 the legal practitioner Kenji Kawagoe published his extensive analysis of 68 reported termination disputes involving continuing commercial contracts from the start of the 20th century until 1988. See K.Kawagoe (1988), *'Keizokuteki torihiki keiyaku no shūryō'* (The Termination of Continuing Trade Contracts) 18 *New Business Law (Bekkan)* (Separate Volume); See also Yoshio Itamura (1982), *'Keizokuteki torihiki no chūshi kaijo o meguru mondai'* (Problems relating to the Ending of Continuing Trade), in: *New Business Law,* Vol. 260, p. 8–16, Vol. 261, p. 48–53, Vol. 264, p. 62–70. In these articles Itamura analysed 22 cases.

termination disputes in actual practice. The disputes, which lead to final judgement, are in fact 'unusual' cases.[29]

## 3.2 Validity of the Termination

In order to draw some conclusions concerning the validity of a termination of a distribution agreement in Japan, distinctions have been drawn between contracts of specified duration and those of unspecified duration. Until recently most termination disputes concerned distribution agreements of unspecified duration.[30]

### *Distribution Agreements of Unspecified Duration*

When parties have deliberately made vague party choices the duration of the distribution agreement is usually unspecified. Since it is not required under Japanese law that distribution agreements are put in writing, these may be oral agreements which usually fail to specify the duration of the agreement and have left questions open as how and when to terminate. The relationship between manufacturer and distributor may be based on repeated deals. The proof of transactions having taken place on a repeated and regular basis implies the existence of such a relationship between manufacturer and distributor. When termination disputes involve such agreements manufacturers have sometimes countered any claims by distributors by contending that a formal contract had never been concluded. However, in such cases the Japanese courts considered all the circumstances of the trade relationship and almost always confirmed that a contract had indeed been concluded.[31]

A common approach on the part of the Japanese courts is to require 'unavoidable reasons' *(yamuoenai jiyū)* for any valid cancellation, irrespective of whether the termination was based on a breach of contract or not.[32] Requiring the terminating party to point to an unavoidable reason for doing so allows the court to examine the actual nature of the parties' relationship and evaluate the impact of the cancellation for the distributor. In this way the Japanese

23 This means that most litigated termination disputes have occurred after the manufacturers/ suppliers terminated contracts with their distributors. See H.Nakata (1994), *Keizokuteki baibai no kaishō* (The Termination of Continuing Sales), p. 57–105.

24 Ibid., p. 89–90.

25 V.Taylor (1993), o. c., p. 378.

26 H.Nakata (1994), o. c., p. 105.

27 See Kenji Iwaki (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction), 560 *New Business Law* 10.

28 These expressions are used for various types of continuing contracts and cannot really be defined under case law. However, distribution agreements are often included under these concepts. See H. Nakata (1994), o. c., p. 62–63.

29 K.Kawagoe (1988), o. c., p. 1.

courts tend to protect the interests of distributors for whom the ill effects of the cancellation can be very injurious.

In one famous case, three years into the trade relationship a supplier had cancelled the agreement of unspecified duration for opportunistic reasons. The distributor had obtained an exclusive sales right in a designated area and the supplier had profited greatly from the distributor's expanding sales service and substantial investments. The court held that the principle of good faith dictates that in the absence of any 'unavoidable reasons' making the continuation of the contract extremely difficult, a unilateral termination could not be justified.[33] According to legal scholar, Hiroyasu Nakata, these reasons are not only more serious than a mere breach of contract but also have a much wider range.[34] He distinguishes four categories of decisions in which the court had concluded that unavoidable reasons existed.

### *Serious Breach of Contract*

In the first category of decisions the unavoidable reasons are evidenced by a serious breach of contract. This applies to cases where the distributor fails to perform a duty or obligation which is essential to the contract. For example, this may be the non-payment of deliveries by the distributor.[35] This is concurrent with Article 541 of the Civil Code, which requires that the manufacturer must demand that it be paid within a certain period of time and if the distributor has failed to pay within such period, the manufacturer is entitled to terminate.

### – Breakdown of the Relationship of Trust

In the second category, a 'breakdown of the relationship of trust' *(shinrai kankei hakai)* may satisfy the requirement of unavoidable reasons. This concept has been developed through judicial precedent and legal theory.[36] It means that contracts can only be cancelled when the relationship of trust between both parties has broken down. On the one hand, this can justify an early termination of the contract when the relationship has deteriorated and when it cannot be expected that the transaction be preserved until the agreed termination date. On the other hand, cancellation on the agreed termination date may be prevented where 'trust' between the parties still exists. Initially this concept was applied only in the context

30 H.Nakata (1994), o. c., p. 87.

31 Ibid., p. 64. See, for example, *Miko Kakō* v. *Rikō Sangyō,* 1020 *Hanrei Jihō* 64 (Tokyo District Court, 26 May 1981); 1144 *Hanrei Jihō* 88, (Tokyo High Court, 24 December 1984); *Jeans case,* 1490 *Hanrei Jihō* 111, (Osaka District Court, 21 June 1993).

32 This concept is borrowed from Articles 628 (Employment), 651 (2) (Mandate), 663 (2) (Bailment) and 678 (2) (Partnership) of the Civil Code on the basis that these types of contract are analogous to continuing contracts.

For example Article 628 on Employment Contracts reads: 'Even where a period for the service has been fixed by the parties, either party may, if any 'unavoidable cause' exists, immediately terminate the contract: however, if such cause has arisen by the fault of one of the parties, such party is liable for compensation for damages to the other party'. (EHS translation. p. 104).

of the termination of leases[37] but later this was applied analogously by the courts to other types of continuing contracts like distributorship agreements.

The courts have considered the relationship of trust to have broken down in such cases where the distributor has unilaterally changed the terms of settlement,[38] when he was convicted of a crime,[39] where he was not co-operative in finding an adequate method of payment,[40] or when the distributor had resold products from another supplier on which he had attached labels from the products of his regular supplier.[41]

In one case the Japanese court found that there had been a disruption in the distribution channel which was sufficient to constitute a breakdown in the parties' trust relationship. It approved of an immediate cancellation of a consignment sales contract by a major wholesaler of books, when his trading partner, an intermediate book wholesaler, had thrown his distribution system into disorder because he wished to establish a sales channel for a rival company of the wholesaler. He had spread rumours that the wholesaler would become insolvent.[42]

– Anxiety concerning the Reliability of the other Party

In the third category 'anxiety concerning the reliability' *(shinyō fuan)* of the distributor constituted unavoidable reasons for cancellation. In these cases the courts had first concluded that there were objective factors for such anxiety. In one case in which the court denied the high probability of non-payment, it held that such probability should not be judged by the subjective judgement on the side of the supplier.[43]

However, according to the courts such anxiety in itself did not entitle manufacturers to terminate the contract. Only after the distributor had not responded to requests by the supplier for clarification of his financial affairs, a change in terms of settlement or the provision of securities, was the termination held to be valid.[44] In one case a distributor was

33 See *Hayashiya K.K. v. Y.K. Yamamotoyama,* 634 *Hanrei Jihō* 50 (Nagoya High Court, 29 March 1971).

34 H.Nakata (1994), o. c., p. 390.

35 1132 *Hanrei Jihō* 152 (Nagoya District Court, 21 February 1984).

36 This concept has been widely discussed in Japan. Kenji Kawagoe is critical of this concept and he contends that it is too vague and subjective. See K.Kawagoe (1988), o. c., p. 48–50, 64–66. According to legal scholar Yoshihisa Nōmi this concept is slightly different from the concept of good faith and has a particularly Japanese characteristic. See Y.Nōmi (1998), *'Kisei kanwa jidai ni okeru hō no jitsugen' (Law Enforcement* in a Period of Deregulation), 632 New Business Law 13.

37 This concerned the cancellation by the lessor based on Article 612 of the Civil Code, which gave the lessor the right to cancel when the lessee had sub-leased without consent. The courts, however, denied this right in cases where the acts of the lessee had not really caused the parties' trust relationship to break down. See, for example, 9 *Minshū* 979 (Supreme Court, 25 September 1953). See also *Minshū,* Vol. 18, No. 6, p. 1220 (Supreme Court, 28 July 1964). In this case the court found that for a valid cancellation a breach of contract is not sufficient. A breakdown of the relationship of trust is required.

38 180 *Hanrei Taimuzu* 123 (Yokohama District Court, 6 April 1965).

in a financially difficult position and the manufacturer requested several times some security for payment which the distributor failed to give. The court held that the termination of the distribution agreement was not a surprise to the distributor even though no notice was given.[45]

– Change of Circumstances

Finally, in the fourth category a change of circumstances may satisfy the unavoidable reasons requirement. This applies to circumstances which occur due to events beyond the control of either party to the contract. For example, when a sudden change in the economy has forced the parties to negotiate a new price without success, the courts have allowed the cancellation of the distribution agreement. In one case after the Oil Crisis in the 1970s the price of raw material had skyrocketed and the supplier demanded an increase in price. In response the distributor decided he would pay no longer. The court allowed the supplier to cancel the contract.[46]

In summary, it can be concluded that these concepts of unavoidable reasons or a breakdown of the relationship of trust are very flexible tools as far as the courts are concerned which can be accommodated within the general Civil Code principle of good faith.[47]

Another approach of the courts, which is less common, is not to require any unavoidable reasons but to validate the unilateral cancellation as long as a reasonable advance notice[48] or sufficient compensation[49] has been provided. However, it remains doubtful whether the provision of advance notice or compensation without disclosing the reason for termination is sufficient for a valid termination. It must also be noted that in actual practice disputes surrounding notice periods are rare simply because suppliers seldom justify the cancellation by the single fact that sufficient advance notice was provided. Termination disputes which lead to litigation are usually those in which the supplier wanted to cancel immediately. In those cases the dispute is focused on the reasons given for the immediate cancellation.[50]

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39 *Kono Tarō v. Hokkaidō Shinbunsha K.K.,* 881 *Hanrei Jihō* 134 (Sapporo District Court, 30 August 1977).

40 In this case the distributor had paid by means of a promissory note on which he was expected to default and for which the place of payment was a bank which was not involved in the trade relationship. He had not co-operated in the subsequent negotiations on the revision of the method of payment. See 140 *Hanrei Taimuzu* 127 (Supreme Court, 13 December 1962).

41 437 *Hanrei Taimuzu* 139 (Tokyo District Court, 26 September 1980).

42 *Nihon Shoseki Hanbai K.K. v. Kōki Shuppan Hanbai K.K.,* 1126 *Hanrei Jihō* 42 (Osaka High Court, 14 February 1984).

43 See *K.K.Advance v. K.K.Token,* 880 *Hanrei Jihō* 51 (Tokyo District Court, 22 July 1977).

44 865 *Hanrei Jihō* 71 (Tokyo District Court, 22 February 1977); 1087 *Hanrei Jihō* 101 (Tokyo District Court, 3 March 1983); 1389 *Hanrei Jihō* 79 (Tokyo District Court, 20 December 1990).

45 See *Wako Kogyō K.K. v. Meko Kōgyō K.K,* 772 *Hanrei Jihō* 71 (Tokyo District Court, 12 September 1974).

There is a subtle relationship between unavoidable reasons and the provision of an advance notice. The existence of unavoidable reasons may justify an immediate cancellation. By contrast, the provision of a sufficient advance period may soften the requirement of unavoidable reasons.[51]

### *Distribution Agreements of Specified Duration*

So far, termination disputes have almost only involved distribution agreements of unspecified duration, but recently more disputes are related to agreements of specified duration.[52] These agreements are often in writing and include renewal and termination clauses, which are usually advantageous for the manufacturer which has drafted these contracts.[53] The Japanese courts have sometimes invalidated the enforcement of these clauses while using the doctrine of good faith or abuse of right. In some cases the contract could not be terminated in the manner stipulated by the parties to the contract. This occurs in particular in case of a termination of exclusive distribution agreements at short notice.[54]

### *Non-renewal of the Contract*

Distribution agreements often include clauses which serve to automatically renew the agreement unless either party gives notice of its intention not to renew within a specified period of time prior to the expiration of the term. Generally speaking, one characteristic of many of these contracts is that even when there is a fixed duration, renewal will be virtually automatic and in practice such contracts are renewed many times over.[55] To date, termination disputes are rarely triggered by the non-renewal of distribution agreements, but since the 1980s more such termination disputes have appeared.[56] The courts have taken two different approaches in relation to these disputes.

In the first, most common category, unavoidable reasons are required. In many decisions the Japanese courts have held such a non-renewal clause to be unenforceable and these

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46 See 1107 *Hanrei Jihō* 120 (Mito District Court, 5 September 1983). It must be noted that the doctrine of changed circumstances *(jijō henkō no gensoku)* may also be an important doctrine for providing an excuse to terminate the contract. However, the doctrine has been applied in only a limited number of cases. See K.Iijima (1994), *'Jijō henkō no kōka to shite no keiyaku no tekigō to kaijo'* (Termination and Adjustment of the Contract as an Effect of Changed Circumstances), 35 *Tōritsudai Hōgakkai Zasshi* 127.

47 See V.Taylor (1993), o. c., p. 383.

48 *Miko Kakō v. Rikō Sangyō,* 1144 *Hanrei Jihō* 88 (Tokyo High Court, 24 December 1984).

49 126 *Hanrei Taimuzu* 65 (Osaka District Court, 12 October 1961).

50 H.Nakata (1994), o. c., p. 76, 494.

51 Ibid., p. 494–495.

52 Ibid., p. 87.

53 Ibid.,p. 104.

decisions have received wide attention among legal practitioners and scholars in Japan. In these cases it was judged that contracts of a specified duration become contracts of an unspecified duration when the contract has been automatically renewed many times over. This means that the termination can only be valid as long as there are unavoidable reasons for the termination.

– Hokkaidō Tractor case

The most famous example of this approach is the Hokkaidō Tractor case, which has been cited frequently by Japanese legal scholars. In much detail the Sapporo High Court described the circumstances of the parties' relationship which may justify the requirement of unavoidable reasons for a valid termination.

It involved a dispute which arose as a result of a non-renewal of an exclusive distributorship agreement. The facts of the case were as follows: a contract between a manufacturer of farm machinery had been renewed annually over a number of years. The dispute started when the manufacturer no longer intended to continue the trade relationship and in accordance with the termination clause provided three months notice. The distributor contested the validity of the non-renewal and contended that the attempted termination constituted an abuse of right. He filed an application for an injunction in order to prevent the manufacturer from distributing the products through a new distributor.

The Sapporo High Court held that there were no 'unavoidable reasons', which were required for a valid termination of the contract. The court granted the injunction order, which was valid for one year and refused to terminate the agreement between the distributor and the manufacturer. The court interpreted the non-renewal clause in such a way that in the event that continuation of the contract should prove to be 'manifestly unjust' to one of the parties, the other party can only cancel the contract if there are unavoidable reasons. The court considered the circumstances under which the contract had been entered into, the key provisions in the contract and any profit or loss gained or suffered due to nonrenewal.

The court argued that the distributor had made substantial investments on the expectation that the contract would continue and it was difficult to find a new contract partner in the industry, which was very closed due to its distribution structure. The court also took into account that the distribution business is impracticable to run on a one-year basis, because the machines are expensive and it takes time to convince farmers of the advantages of the new machines. Accordingly, the economic loss of the distributor stood in sharp contrast to the profit of the manufacturer which stood to gain unjustly from taking over the market established by the distributor.[57]

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54 See also K.Matsumoto (1996), o. c., p. 494.

55 Veronica Taylor cites the article by Kenji Kawagoe in which he had analysed 157 continuing contracts, most of which contained automatic renewal clauses and 90 percent were in fact renewed. See V.Taylor (1993), o. c., p. 378. She cites K.Kawagoe (1985), *'Keizokuteki keiyaku kankei no shūryō'* (Termination of Continuing Contracting Relationships), 342 *New Business Law* 6,9.

56 H.Nakata (1994), o. c., p. 81.

– Two other important Cases

A similar conclusion was reached in a case where a franchiser had notified a local sub-franchiser that he would not renew the contract after the end of the contractual term of five years. In response, the sub-franchiser applied for a provisional disposition to confirm that the contract was still valid. The Nagoya District Court granted the injunction and held that there were no unavoidable reasons which are required for a valid termination. The court considered the way in which the contract had been concluded and the substantial advertisement costs which had been borne by the sub-franchiser, which had in turn largely contributed to the increase in profits. Furthermore, the franchiser had been strongly involved in the business of the sub-franchiser and there were no examples of other contracts with sub-franchisers which had ended after the expiry of the five-year term.[58]

Finally, the following case is also a good example of this approach. It concerned a contractual relationship of consignment carriage which had been renewed annually over 27 years. The Sendai District Court held that a three-month prior notice not to renew the contract should be construed as a termination notice and was extended by three months. The transporter had made large investments relying on the continuation of this contract and it had been impossible for the transporter to conclude a similar contract with another party. Accordingly, the unilateral termination was very damaging for the transporter.[59]

The second category of court decisions supports the general contract law principle, which determines that a contract ends when the contract period has expired and has not been renewed by one of the parties. In some cases the Japanese courts have simply decided that one party may terminate the contract after the contract period has expired, although the other party wishes to renew it.[60]

– Shanson Cosmetics case

In one recent decision of the Tokyo High Court the facts of the case were as follows: A company had concluded a consignment sales contract with a distributor for the sale of cosmetics. The contract had been renewed automatically every year. After 29 years the contract was revised in that it was now to be automatically renewed for three-year periods if neither party objected thereto. The dispute started when the distributor began to slander the cosmetic products of the company and also started to sell health-food products, while

57 *Hokkaidō Ford Tractor K.K. v. Minoru Sangyō,* 1258 *Hanrei Jihō* 76 (Sapporo High Court, 30 September 1987).

58 *Hokka Hokka v. Human Life,* 1377 *Hanrei Jihō* 94 (Nagoya District Court, 31 August 1990). This decision was based on a complaint *(igi mōshitate)* against an earlier decision of the same court in which it had held for the franchiser while determining: 'as long as there are no special circumstances under which the non-renewal of the contract violates the good faith principle and the public order or good morals, the contract ends when the period expires'. See 1377 *Hanrei Jihō* 473 (Nagoya District Court, 31 October 1989).

making use of the sales channels of the company. The company thereby refused to renew the contract after the first three-year period had expired. The Tokyo High Court validated the non-renewal of the contract not because of the slandering or the breach of contract, but for the simple reason that the contractual term of three years had expired. The court did not hold that the contract had been transformed into a contract of an unspecified duration.[61]

### *Intermediate Termination*

#### – Intermediate Termination Clause

Many distribution agreements of specified duration include an intermediate termination clause. Usually these concern standard-form provisions which entitle one of the parties to cancel immediately in case of insolvency or a structural suspension of payments on the part of the other party. These may also include obligations, which form the distribution system in order to control the quality and service offered. An example is a duty to provide for proper after-service, any breach of which would evenly strike at the heart of the agreement. A typical distribution agreement may stipulate that in the event that one of the parties has failed to perform any of the duties or obligations under this agreement the other party may terminate the contract immediately or at very short notice before the expiry of the contract period.

However, the Japanese courts have usually required more than a mere breach of contract provision before validating such intermediate cancellation. Similar to contracts of unspecified duration the courts have used concepts such as 'unavoidable reasons'. However, in practice the courts have almost always validated such intermediate termination. For example, an immediate termination by a supplier was validated because the terminating party obviously had great anxiety regarding the reliability of the distributor,[62] because the distributor had seriously violated contractual terms by non-payment[63] or had caused a breakdown of the parties' trust relationship.[64]

#### – The 'Notice at any time' Clause

Distribution agreements of a specified period also often include a provision stating that, this period notwithstanding, either party may effect termination by giving notice of, for

59 Although this case did not involve a termination of a distribution agreement it is worth describing. See 553 *Hanrei Jihō* 126 (Sendai District Court, 30 September 1994).

60 See for example, 981 *Hanrei Jihō* 87 (Tokyo District Court, 29 May 1980).

61 See the *Shanson Cosmetics case,* 811 *Hanrei Taimuzu* 149 (Tokyo High Court, 20 October 1992). This case is discussed by Kenji Iwaki, Kenji Kawagoe, Kōji Shindō and Noboru Kashiwagi (1995), in: *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction), 560 *New Business Law* 15–16.

example, sixty days, without having to disclose any reason therefor. In this way parties maintain flexibility and can terminate the contract if circumstances have changed.[65] However, in actual practice only in exceptional cases can parties use these clauses to terminate a distribution agreement.[66] Such 'notice at any time' clauses, which enable manufacturers to terminate at will without providing any reason therefor may well be held to be unenforceable by Japanese courts. They have taken two different approaches in order to restrict the enforceability of such clauses.[67]

In some decisions the courts have held that only as long as there are 'unavoidable reasons' can such clauses be enforced.[68] By contrast, in other decisions the courts have found that unavoidable reasons are not a necessary requirement for a valid termination. In this approach the courts hold that in principle such clauses are valid but there needs to be an investigation into whether the enforcement of such a clause does not violate the principle of good faith or constitute an abuse of right.[69] This latter approach has gained ground because of an influential decision by the Tokyo High Court in which it concluded that unavoidable reasons are not a necessary requirement for a valid termination. It held that in view of the freedom of contract principle a party does not have to give a reason for the termination based on such a clause. The termination is only invalid if it violates the principle of good faith,

62 The court argued that the financial standing of the distributor and his reputation among his trading partners had worsened. The court held that by continuing the trade relationship the manufacturer could incur heavy losses. 1054 *Hanrei Jihō* 92 (Tokyo High Court, 25 August 1982).

63 In one case the distributor had regularly paid too late, slandered the manufacturer and his products and even urged the other distributors of the manufacturer to buy such products from other manufacturers. 1105 *Hanrei Jihō* 70 (Tokyo District Court, 8 September 1983).

64 A distributor had concluded two different contracts for the distribution of two pharmaceutical products. Thirty-seven years into the agreement the distributor breached one of the contracts because it had bought similar pharmaceutical goods from another company which was forbidden. The supplier terminated both contracts immediately. Although there was no intermediate termination clause in the second contract, the court also validated the cancellation of this contract because the distributor had breached the 'trust' of the supplier. 862 *Hanrei Jihō* 87 (Osaka District Court, 27 January 1977).

65 See Haruhiro Nakatsu (1994), *'Dokkinhō to keiyaku no jiyū'* (The Anti-monopoly Act and the Freedom of Contract), 554 *New Business Law* 23.

66 Kenji Kawagoe considers such termination to contradict with the general practice of maintaining continuing commercial relationships. See K. Kawagoe (1994), *'Shiseido Tokyo hanbai jiken kōsoshin hanketsu no gaiyō'* (An Outline of the Appeal Decision in the Case involving the Shiseido Tokyo Sales Company), 555 *New Business Law* 17–18.

67 See Hiroyasu Nakata (1995), *'Keizokuteki baibai keiyaku no kaishōsha no ito'* (The Intention of the Party Terminating a Continuing Sales Contract), 569 *New Business Law* 10–11.

68 See for example the *Aloins case,* 1612 *Hanrei Jihō* 62 (Osaka High Court, 28 March 1997); See also *Shiseido v. Fujikihonten,* 1474 *Hanrei Jihō* 25 (Tokyo District Court, 27 September 1993); the same case on appeal: 1507 *Hanrei Jihō* 43 (Tokyo High Court, 14 September 1994). As will be described in the following two chapters, on further appeal the Supreme Court has confirmed this decision. However, the decision was entirely based on anti-trust law. The Supreme Court did not refer to the question whether unavoidable reasons are required or not. See *Shiseido v. Fujikihonten,* 1664 *Hanrei*

constitutes an abuse of right or violates public order and good morals because it violates a compulsory law.[70]

### *Compensation and Notice Requirements*

#### – Notice Requirement

The reason for the cancellation of a distribution agreement is an important factor for determining whether a notice period is required or not. In one case the Osaka High Court judged that, depending on the nature of the contract, in the absence of a serious reason preventing the continuation of the contract, a reasonable notice period will be required for a valid termination of a continuing contract.[71] Generally speaking, what constitutes a reasonable period of notice cannot be fully deduced from case law. This depends on the particular circumstances of the case. Some practitioners argue that as a general rule for most product categories a period of six months would seem to be commercially reasonable in the event that investments have not been substantial.[72] However, most practitioners suggest that as a general rule notice should be given by a manufacturer at least one year prior to the termination date.[73]

#### – Compensation

The distributor can bring an action before the civil court demanding compensation, while contending that the suspension of supplies and the cancellation of the contract were illegal. This course of action is taken in most cases.[74] Even where the manufacturer has given a reasonable notice the court may still award compensation to the other party.[75]

Under the Japanese Civil Code, claims for damages are limited to those arising from non-performance or a tortuous act. However, even where non-performance by the supplier is

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*Jihō* 3 (Supreme Court, 18 December 1998).

69 *Market management case,* 1030 *Hanrei Jihō* 15 (Tokyo District Court, 25 August 1981); *Yasuda fire insurance agent case,* 325 *Hanrei Taimuzu* 313 (Yokohama District Court, 28 May 1975). The latter case concerned a termination of an insurance agency contract; *Kao v. Egawakikaku,* 1500 *Hanrei Jihō* 3 (Tokyo District Court, 18 July 1994).

70 *Kao v.Egawakikaku,* 1624 *Hanrei Jihō* 55 (Tokyo High Court, 31 July 1997). As will be described in the following two chapters, on appeal the Supreme Court has confirmed this decision. See *Kao v. Egawakikaku, 1664 Hanrei* Jihō 14 (Supreme Court, 18 December 1998).

71 *Nihon Shoseki Hanbai K.K. v. Kōki Shuppan Hanbai K.K.,* 1126 *Hanrei Jihō* 42 (Osaka High Court 14 February 1984). In this case the court concluded that there were unavoidable reasons and it approved an immediate cancellation by the supplier.

72 Keiji Matsumoto (1996), o. c., p. 494.

73 See Y.Hanamizu (1988), Termination of Distribution Agreements in Japan', in: *Legal Aspects of Business Transactions and Investment in the Far East,* D.Campbell and A.Wolff (eds.), p. 48. See also Kenji Kawagoe (1986), *'Keizokuteki keiyaku kankei no shūryō'* (Termination of Continuing Contracting Relationships), 345 *New Business Law* 34.

not evident the courts may still recognise a right to claim compensation, which can be explained as an application of the Civil Code principle of good faith.[76] In most cases the court is asked to determine the quantum of compensation payable. When calculating the amount of compensation in most cases courts base the awards on projected profits. The actual amounts awarded vary. The courts may examine the efforts and investment of the distributor to develop business, the amount of time it will take for the distributor to convert to another product line and the percentage of the distributor's business that the discontinued line of business comprises. However, the overall tendency appears to be that damages are calculated according to a projected profit-prediction for the following year.[77]

In one famous case, three years into the trade relationship a manufacturer terminated a distribution agreement for opportunistic reasons after having profited from the sales activities of the distributor. The distributor had obtained an exclusive sales right in a designated area and had put great efforts into expanding the sales channel while investing heavily in the operation of sales and advertising. The court held for the plaintiff and awarded damages equalling one year's net profits. The court had taken into consideration the amount of investments made by the distributor and the time required to convert to another product line and to replace the supplier.[78]

Sometimes courts award so-called 'reliance interest' *(shinrai rieki),* which is the damage suffered as a result of believing that the contract will continue. This also includes what could have been avoided had the party known that the contract would not continue. This notion is not always very clear but it often concerns the amounts not recovered from concrete investments. These may be the costs incurred in changing furniture,[79] in producing catalogues which have become obsolete,[80] in sales activities or in the employment of personnel.[81]

74 See H.Nakata (1994), o. c., p. 88.

75 See *Miko Kakō K.K. v. Rikō Sangyō,* 1144 *Hanrei Jihō* 88 (Tokyo High Court, 24 December 1984).

76 See K.Kawagoe (1986), *'Keizokuteki keiyaku kankei no shūryō'* (Termination of Continuing Contracting Relationships), 345 *New Business Law* 33.

77 H.Nakata (1994), o. c., p. 88. See 1020 *Hanrei Jihō* 64, (Tokyo District Court, 26 May 1981); 286 *Hanrei Jihō* 25, (Tokyo District Court, 13 December 1961); 1417 *Hanrei Jihō* 80 (Tokyo District Court, 19 July 1991).

78 *Hayashiya K.K. v. Yamamotoyama,* 634 *Hanrei Jihō* 50, (Nagoya High Court, 29 March 1971).

79 126 *Hanrei Taimuzu* 65 (Osaka District Court, 12 December 1971).

80 298 *Hanrei Taimuzu* 395 (Osaka District Court, 8 December 1972).

81 880 *Hanrei Jihō* 51 (Tokyo District Court, 22 July 1977).

## 3.3 Summary

The court decisions are not univocal and can be roughly divided into two categories.

In the first category of decisions, which are by far the most common, beyond the actual terms of the contract, the courts give substantial consideration to circumstances and conditions not expressly stated or disclosed in the contract itself. Separate grounds for termination are required without which the cancellation is not valid. This means that in this category the operative area of termination can be much more restricted. The determining factor in many of these decisions is whether 'unavoidable reasons' exist for the termination, a concept which can be accommodated within the general Civil Code principle of good faith. This concept remains fairly vague, but it enables the courts to also take the parties' subjective circumstances into consideration.

In case law these unavoidable reasons are often derived from a serious breach of contractual obligations, the breakdown of the parties' trust relationship, anxiety concerning the other parties' reliability or a change in circumstances.

Because this requirement is applicable for the termination of an agreement of unspecified duration as well as an agreement of specified duration, it means that in this category the courts do not make such a broad distinction between distribution agreements of specified and those of unspecified duration.[82]

However, according to Hiroyasu Nakata the seriousness of the required unavoidable reasons varies. A non-renewal of a distribution agreement is more easily validated by the courts than a termination of an agreement of unspecified duration. For example, there may be cases where a change in business policies or economic conditions may constitute unavoidable reasons.[83]

In turn, terminations of an agreement of unspecified duration are more readily held to be valid than terminations before the expiry of an agreement of specified duration.[84] When distribution agreements are terminated before the expiry of the fixed term, the distributor needs more protection and the existence of unavoidable reasons is less easily acknowledged. In such cases before concluding whether unavoidable reasons exist, the courts also take the behaviour of the terminating party into consideration. They want to discover, for example, whether it requested the distributor to repair performance and whether it demanded clarification as to his financial affairs or a change in trade policies before terminating the contract.[85]

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82 H.Nakata (1994), o. c., p. 82.

83 Ibid., p. 493.

84 Ibid., p. 392 ; Also H.Nakata (1995), *'Keizokuteki baibai keiyaku no kaishōsha no ito'* (The Intention of the Party Terminating a Continuing Sales Contract), 569 *New Business Law* 9–10.

85 H.Nakata (1994), o. c., p. 492.

86 See Takashi Uchida (1993), *'Gendai keiyakuhō no arata na tenkai to ippan jōkō'* (General Clauses and

This category of decisions in which courts take more interest in the relational aspect of the distribution relationship and in which courts basically respect the continuation of such contracts has become more pronounced since the 1970s.[86] Particularly the fact that the distributor had made substantial investments based on the expectation that the contract would continue has been an influential factor for the courts to justify their requirement of unavoidable reasons for a valid termination.[87]

In the second category of decisions the Japanese lower courts tend to adhere to the logic of classical contract law with an emphasis on the principle of freedom of contract. These kinds of decisions seem to have gained some ground recently. Both the recent decisions by the Tokyo High Court in relation to disputes in the cosmetics industry are a good example. In both these decisions the non-renewal of the contract and the termination based on a 'notice at any time' clause was easily validated.

Although this disparity may lead to different results, this is not always the case. Despite different theories, in practice both categories of decisions have often led to the immediate termination of the distribution agreements. In most cases the courts have imposed an obligation to provide notice to the other party or the obligation to pay compensatory damages. For example, in case of a unilateral termination of a distribution agreement of unspecified duration in the first category of decisions, the courts have invalidated the termination because there were no unavoidable reasons and they awarded damages calculated according to a projected profit-prediction for the following year. In the second category the courts have validated the termination without requiring unavoidable reasons to be present, but sometimes they have still demanded the terminating party to provide one-year's notice. Accordingly, these two different approaches do not always lead to different results.[88]

## 4
## LEGAL LITERATURE

In legal literature a similar dichotomy exists. Japanese legal doctrine on the termination of continuing contracts is separated into two groups.

The first most common category of court decisions has received the widespread support of many legal scholars who want unilateral cancellation of continuing contracts, such as

New Developments in Contemporary Contract Law), 516 *New Business Law* 26.

87 Tadashi Shiraishi (1998), *'Keiyakuhō no kyōsō seisakuteki na ichi danmen'* (One Aspect of Contract Law in its Policy on Competition), 1126 *Jurisuto* 125.

88 K.Kawagoe (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction) 560 *New Business Law* 11. For example this applies to the two recent Tokyo High Court decisions as regards the terminations by large cosmetics manufacturers based on the 'notice at any time clause'. Despite different approaches they reached similar results. These cases will be described in much detail within the next two chapters.

distribution agreements, to be subjected to strict limitations. Accordingly, they favour concepts such as 'unavoidable reasons' and a 'breakdown of the relationship of trust'. Many legal scholars who have studied the termination of continuing commercial contracts have pointed to the need to protect the distributor as the weaker party and to protect his reliance upon the continuation of the contract.[89] The predominance of small businesses in the distribution and retail sectors of the Japanese economy may have influenced this judicial attitude to protecting the weaker party.[90]

It must be noted that the first category of decisions are explained and supported by many legal scholars who have started to move away from adhering to the classical contract model when discussing the termination of continuing contracts. Several legal scholars have started to consider only the business relationship itself which has been terminated, without paying any attention to the formal terms of the underlying contract.[91]

For example, Takashi Uchida, influenced by MacNeil's concept of relational contracts,[92] has presented a new model of post-modern contract law, which is a reaction to the classical contract model. His purpose was to shed new light on Japanese contract law through a study of the development of recent contract theory in the US. He asserts that the dualism of contract norms supposed in the relational contract theory of Ian MacNeil may be a suitable theoretical model for the dualism in Japan between law in the books and living law.

Justifying the extended application of the good faith doctrine in Japanese contract law, he maintains that this can be interpreted as the absorption of Japanese relational contract norms into positive contract law. He suggests that the decisions, which prohibit the cancellation of continuing contractual relationships without good reason and respect the continuation of the contract, are in accordance with the strong tendency among Japanese businessmen to maintain continuing trading relationships. However, he explains that these decisions are not based on a protection of the weaker party but are rather seen as expressing an underlying 'principle of continuity' *(keizokusei genri)* which, according to him, is a

89 See H.Nakata (1994) o. c., p. 51 who cites Eiichi Hoshino in: *'Dairiten tokuyakuten keiyaku no kenkyū' (Investigation into Distri*bution Agreements), 144 New Business Law (Zadankai) 28–29 (1977) and K.Kawagoe (1988), 18 *New Business Law (Bekkan)* (Separate Volume), p. 10–11. Kawagoe contrasts this protection of the weaker party with the concept of free competition in which the principle of freedom of contract is included.

90 See K.Kawagoe (1988), o. c, p. 10–11.

91 See for example H.Nakata (1994), o. c., p. 56, 107. He also gives a list of such studies by other legal scholars on p. 53.

92 See for example I.Macneil (1980), *The New Social Contract: An Inquiry into Modern Contractual Relations,* 1980.

93 Uchida points to a possibility of a distinctive Japanese relational contract theory which is based on the Japanese legal culture of contracts. See Takashi Uchida (1990), *Keiyaku no saisei* (The Rebirth of Contract).; T.Uchida (1993), *'Gendai keiyakuhō to arata na tenkai to ippanjōkō'* in: *New Business Law V*ol. 514–517; See also T.Uchida (1998), *'Kisei kanwa to keiyakuhō'* (Deregulation and Contract Law), 632 *New Business Law* 23. His theory has led to great controversy within Japan. For a critical assessment

widespread norm within continuing trade relationships. He asserts that this principle has first been applied to labour contracts but has spread to other continuing contracts such as distribution agreements. According to Uchida, the famous decision in the Hokkaidō Tractor Case is an example of this new development in judicial decisionmaking.[93]

By contrast, recently more legal scholars have begun to support the second category of court decisions which favour a stronger emphasis on contract terms and the logic of classical contract law. They rationalise the judicial intervention in the freedom of contract and contend that this principle must be respected as far as it does not clearly violate any mandatory Code provisions or the public order. They emphasise the value of free competition and respect for the contractual clauses as agreed upon by the parties.[94]

Some of these legal scholars point to the inevitable increase in the cancellation of commercial contracts triggered by the current restructuring of Japanese distribution systems, caused by strong pressures to lower prices. This would then lead to changes in attitudes towards the termination of continuing contracts. They argue that the emphasis on the need to protect the weaker party may gradually become weaker.[95]

Other legal scholars point to the current efforts towards deregulation which requires further emphasis on the principle of freedom of contract. They contend that the notion of restricting the termination of contracts by large manufacturers has been influenced by traditional thinking from before the World War II. The period before the War saw the beginning of a strong tendency to place more emphasis on the protection of the weaker party than on the freedom of contract within continuing contracts such as lease contracts. During that period many feudal elements existed within lease and labour contracts. These elements governed the relationship between landlords and tenants which caused many societal problems and therefore resulted in a strong need to protect tenants.[96] For a similar reason legislation such as the Land and House Lease Law was eventually enacted. However, these scholars contend that in a civil society and market economy, respect for the freedom of enterprise and the freedom of contract is necessary for the development and the formation

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in English of this theory, see Luke Nottage (1997), 'Japanese contract law, Theory and Practice: Plus ça change plus c'est la même chose?', in: V.Taylor (ed), *Asian Laws through Australian Eyes,* p. 324.

94 See Kenji Iwaki (1995), *'Kakaku hakai genshōka no keizokuteki torihiki',* 560 *New Business Law* 10; See also H.Nakata (1995), *'Keizokuteki baibai keiyaku no kaishōsha no ito'* (The Intention of the Party Terminating a Continuing Sales Contract), 571 *New Business Law* 16–17.

95 Kenji Iwaki and Noboru Kashiwagi (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction), 560 *New Business Law* 10 and 561 *New Business Law* 37.

96 See for example about this period and the related problems J.O.Haley (1991), *Authority without Power—Law and the Japanese Paradox,* p. 89–90.

97 See Hiroshi Iyori (1997), *'Tokuyakuten keiyaku no nin'i kaiyakuken to hanbai nettowāku shisutemu'* (The Right to Terminate a Distribution Agreement at will and a System of Network Sales), 627 *New Business Law* 52; Also Hiroshi Iyori (1997), *'Dokusen kinshi seisaku to dokusen kinshihō'* (Antimonopoly Policy and the Anti-monopoly Act), p. 621, 827.

of a modern society. The current deregulation efforts also presuppose such a development and an emphasis on such freedoms.[97]

Finally, attention must also be drawn to the current deregulation efforts in relation to the Land and House Lease Law and the Employment Standards Law, which are supported by many scholars, mainly economists. In order to promote the working of the market economy there have been proposals to abolish some of the provisions in these laws, including those which restrict the unilateral termination of these contracts. In order to increase the supply of available housing they criticise the clause which protects tenants against termination without a good reason. In case law the courts have often ordered house owners to pay compensation for removal in order to supplement the required good reasons. This has created a great deal of insecurity among house owners who cannot predict whether they must pay compensation or not and therefore they have hesitated in leasing their property.

Similarly they criticise some of the clauses in the Employment Standards Law which lessen the possibilities to terminate employment contracts. This creates problems for companies, which want to become more flexible during the current economic slump.[98]

This all implies a move towards the classical freedom of contract principle[99] and may also have a subtle impact on the judicial approach to the termination of distribution agreements.

## 5
## A BRIEF COMPARISON WITH THE DUTCH JUDICIAL APPROACH

When comparing the Japanese approach with the Dutch approach, the results are somewhat comparable. As in Japan, the solutions for the problems caused by the termination of distribution agreements have been mainly provided by case law. This is in the absence of Code provisions on distribution agreements and against the background of often deliberately vague party choices. Dutch case law also shares many similarities with its Japanese equivalent. First, the Dutch courts also primarily apply the good faith doctrine when they deliver decisions in termination disputes. Article 6:248 of the Dutch Civil Code, in which this doctrine is laid down, stipulates that the legal consequences of a distribution agreement are determined by law, the nature of the agreement and trade usage when the contract itself does not provide for these consequences.[100] Just as in Japan, in Dutch case law it is very

98 See for these proposals by economists, Takashi Uchida (1998), *'Kisei kanwa to keiyakuhō'* (Deregu lation and Contract Law), 632 *New Business Law* 17–21.

99 Takashi Uchida, however, asserts that such deregulation cannot justify a move back to classical contract law. 'Principles of continuity' which protect reliance upon the continuation of the contract can also be explained in logical economic terms. See T.Uchida, Ibid., p. 22.

100 See on Article 6:248 for example M.W.Hesselink (1999), *De Redelijkheid en Billijkheid en het Europese Privaatrecht* (Reasonableness and Fairness and European Private Law) (PhD Thesis, Utrecht).

important that the contract is a continuing one and the Dutch courts have also often protected the distributor while applying the principle of good faith.

Also in the Netherlands, decisions have mostly been rendered by the lower courts and have not been univocal. Furthermore, the requirement of a good reason for a valid termination has also been controversial in Dutch law.

However, despite similarities in legal results, there are important differences in the method of judicial reasoning. Although Dutch courts also readily set aside the termination clauses agreed upon, it seems that they pay more attention to the contents of the underlying formal contractual terms. For example, more focus is directed to the distinction between contracts of specified duration and those of unspecified duration when considering all the relevant circumstances of the case. Furthermore, Dutch courts more clearly distinguish the differences among the various types of contracts within the Dutch distribution sector. For example, they draw a more clearly defined distinction between the termination of a distribution agreement and a commercial agency agreement.

One other difference may be that, compared to Dutch law it seems that in their judicial reasoning the Japanese courts have often gone further in the requirement of a good reason for the termination, thereby favouring the continuation of the contract. This can be illustrated by the fact that Japanese courts often use concepts such as a 'breakdown of the relationship of trust' and 'unavoidable reasons' which do not exist in Dutch case law.

# 6
# BARRIERS TO LITIGATION

## 6.1
## Introduction

Before drawing any conclusions about the extent to which distributors are protected by contract law against unilateral terminations of distribution agreements, it is necessary not only to look at the law according to the book but also at the political and economic context of the law such as the ease of access to the civil courts.[101] Therefore I will also describe the barriers to litigation in Japan.[102] Furthermore, when comparing the Japanese judicial approach with that of the Netherlands, not only the contents of the case law but also the

101 Annette Marfolding (1997), 'The Fallacy of the Classification of Legal Systems: Japan Examied', in: V.Taylor (ed.), *Asian Laws Through Australian Eyes,* p. 26.

102 For a critical view of the existing barriers see Y.Watanabe, S.Miyazawa, S.Kisa, S.Yoshino and T. Sato (1994), *Tekisutobukku gendai shihō* (Textbook on the Contemporary Administration of Justice), p. 22–34.

103 See E.Blankenburg and F.Bruinsma (1994), *Dutch Legal Culture,* p. 4.

104 Still, in proportion to the population there are more judges and attorneys in the Netherlands. In 1995 in the Netherlands there was a total of 1322 judges and 1417 substitute judges (total 2,739).

ease of access to the courts needs to be studied. Despite a certain extent of convergence of sources of law and case law, actual living law might be different. This might put my Japanese findings into perspective.

An interesting detail is that comparisons in a wider international context have shown that after Japan, which in general shows the lowest litigation rates, the Netherlands is in second place as a country where people handle their disputes without resorting to litigation.[103] This corresponds to the comparatively small size of the legal profession in both countries.[104]

However, as will be described below there are some important differences between both countries in the ease of access to the civil courts which leads to the conclusion that Japanese distributors face more barriers in taking their disputes to court. Major differences are not found in the barriers to initiating a full procedure at the District Court which are of a comparable nature, but rather in the lack of a well functioning alternative injunction procedure in Japan. In the Netherlands the alternative summary proceedings play a much more important role than their counterpart in Japan.

## 6.2 Full Civil Procedure

When filing suit against the supplier it is against the background of the following problems that Japanese distributors decide whether or not to commence and continue legal proceedings against their suppliers. The first barrier, which has often been cited by the critics of the Japanese judicial system, are the inherent delays which are caused by civil

Dutch attorneys have just reached the 10,000 mark. In 1994 the Japanese judges in the courts of first instance numbered 2,200. Currently, attorneys number approximately 18,000. See J.Davis (1996), *Dispute Resolution in Japan,* p. 80.

105 See J.O.Haley (1978), The Myth of the Reluctant Litigant', 4 *Journal of Japanese Studies* 359–390. In Japan the average number of new lawsuits filed each year with each trial judge is 1100. See J. Davis (1996), o. c., p. 80. J.Davis also cites Hiroshi Oda in his book on Japanese law who reported that a survey of citizens indicated that 85 percent of the people that responded felt that litigation took too much time. See also A.Marfolding who compares Japanese civil procedural rules with the German system which initially had a strong influence on Japan. She concludes that they are divergent to a significant degree, See A.Marfolding (1997), o. c., p. 38–46.

106 Changes have been widespread but most notable are improvements in small claims proceedings, the preliminary proceedings for modifying matters under court review, modifications in the treatment of evidence at oral hearings in trial proceedings and the expansion in the scope of documents subject to court order for submission. See Tatsuo Ikeda (1998), 'Recent Developments in the Japanese Civil Judicial System', 45 *Osaka University Law Review* 19–24.

107 Marfolding argues that a reformation of legal rules does not necessarily change the habits of judges and legal practitioners. See A.Marfolding (1997), o. c., p. 45.

108 J.Davis (1996), o. c., p. 253.

109 See E.Blankenburg and F.Bruinsma (1994), o. c., p. 42. According to these scholars the delays are partly caused by the caseload of each judge but also to a large extent by delay tactics on behalf of de

procedural rules and a shortage of judges.[105] It must be noted that many provisions in the new Japanese Code of Civil Procedure which was enacted in January 1998[106] are aimed at removing these problems and confirm some already initiated practices used to expedite the trial, but their influence upon the readiness of distributors to bring an action needs to be awaited.[107]

Particularly for distributors, which often require the damages or supplies at short notice, a speedy outcome is very important. However, compared to the Netherlands the problem of delays is not that much different. In Japan in 1994 the average length of all proceedings was 12 months in the District Courts.[108] This is not very different from the Netherlands where on average it takes a first instance court almost one year to reach a decision.[109]
The second barrier, which has also been frequently cited, is constituted by the litigation costs. Japanese lawyers almost always use a two-part fee structure: an initiation fee amounting to a certain percentage of the amount claimed which is paid as a non-refundable retainer and an additional fee relating to the value of a successful outcome.[110] In addition, a filing fee is due which is based on the amount of damages claimed.[111] One problem is that in principle in disputes involving contractual and commercial transactions the winning party cannot recover his legal fees from the losing party. This is based on the fact that representation by a lawyer is not compulsory in Japan. This means that a distributor may be burdened with a significant financial risk even for a claim with a high likelihood of success.

Generally speaking, litigation costs may not turn out to be so very different from such costs in full procedures in the Netherlands. First, in the Netherlands hourly fees are billed which makes litigation for small amounts unattractive and the costs somewhat unpredictable. Furthermore, this promotes delay tactics on behalf of the defendant because further action means higher bills.[112]

Second, although Dutch courts usually order the loser to pay the winner's costs, this almost never covers the entire legal fees.[113] However, one difference with the Netherlands

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fendants. Recently in a survey among Dutch citizens there was also much criticism of the delays in full procedures. See Nederlands Juristen Blad (ed), (1998), *Knelpunten in de rechtspraak* (Bottle-necks in Case Law) in: *Nederlands Juristen Blad (NJB)* 23, p. 1057–1059; and Nederlands Juristen Blad (ed) (1998), *De traagheid van de civiele rechtsgang* (The Slowness of Civil Procedure), in: *NJB* 44, p. 2048.

110 J.Davis (1996), o. c., p. 364. There are some Bar Association fee schedules but percentages are negotiable and such schedules are only taken as a starting point.

111 This fee starts at 1 percent of the first 300,000 Yen of damages claimed, and drops to 0.8 percent of the amount claimed between 300,000 and 1 million Yen and progressively to 0.2 percent of amounts over 1 billion Yen. Although in principle these costs are paid by the losing party, in practice the court determines how these costs will be divided among the parties.

112 See E.Blankenburg and F.Bruinsma (1994), o. c., p. 42.

113 Ibid., p. 8. In the recent survey in the Netherlands particularly the medium and small sized companies complained about high litigation costs, See *NJB* 23 (1998), p. 1058–1059.

is that in Japan distributors usually do not take out insurance cover for litigation costs, whereas this is a much more common practice in the Netherlands.

## 6.3 Injunction Procedures

When a Japanese distributor wants the delivery of supplies to continue one option is to file for a provisional remedy in addition to, or instead of, a main suit.[114] Ge nerally speaking, the application for injunctive relief is very common in Japan.[115] It even often replaces a main suit because frequently the parties will tend to take the injunction as a final decision in substantive law.

One type of injunctive relief, which can be used by distributors in termination disputes, constitutes the provisional disposition *(karishobun)* that permits the court to establish an interim legal relationship and to grant temporarily all or part of the temporary relief this party is seeking in the lawsuit. In theory a distributor can first demand an injunction to confirm his continuing rights under the agreement. Secondly, he can demand an injunction to order the supplier to deliver the products he had ordered. Thirdly, he may even demand an injunction to confirm the continuing rights under the agreement in the future.

However, in termination disputes distributors have rarely filed such provisional dispositions and in most cases have been unsuccessful.[116] Japanese legal scholars raise doubts about the practicality of the demands for such injunctions.[117] First, these procedures may still take a great deal of time. The court often sits in many sessions and the degree of proof required is not so much different from the degree required in a full procedure.

Second, the Japanese courts lack the required enforcement powers for such injunctions. They do not have any practical means of enforcing those orders and thereby to make the supplier deliver the products to the distributor.

Third, with respect to the first two injunctions it needs to be noted that only when the agreement is interpreted by the court in such a way that every order by the distributor automatically obligates the supplier to accept it, do these injunctions have any real meaning. When in the contractual relationship the supplier has always automatically accepted the distributor's orders for an extended period, this duty to accept the order will more easily be acknowledged.[118]

However, in relation to the third kind of injunction the Japanese courts do not go so far as to confirm continuing rights under the agreement in the future. The Japanese courts find

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114 This kind of provisional disposition is stipulated in the Civil Preservation Act *(Minji hozen hō)* of 1989. This law has replaced the sections on provisional relief that had been contained in the Code of Civil Procedure. In order to obtain a provisional disposition an applicant must show a need for the order and evidence, offering reasonable support for the underlying claim. The court will then usually conduct a hearing on the matter and give the party against whom the provisional disposition is sought an opportunity to show why it should not be granted. If the request for a court injunction is rejected, Article 26 of the Civil Preservation Act enables the applicant to file an objection before the same court *(hozen igi)*.

it very difficult to grant this injunction, because under certain circumstances the supplier must maintain the right to deny acceptance of the order.[119] Furthermore, in contract proceedings the Japanese courts do not usually grant injunctions with regard to future actions.[120]

Finally, it is important to note that Japanese judges in injunction proceedings are usually young and inexperienced and are only beginning their careers in the District Court Section on injunctive relief.

These problems constitute an important difference with the Netherlands where a comparable injunction procedure is very important for distributors in termination disputes. This Dutch summary procedure *(kort geding)* has been frequently used by distributors where they can obtain an 'interlocutory' injunction at very short notice. This rarely takes more than six weeks from start to finish and is very inexpensive. In most of these procedures there is only one oral hearing of the case. The decisions can be based on the credibility of the evidence.[121]

In such procedures Dutch distributors have often demanded specific performance while arguing that the notice period is insufficient. In most cases the objective, a better bargaining position against the supplier, has proved to be effective. It must also be noted that the Presidents of District Courts in these summary procedures have more enforcement powers as regards their injunctions than do the Japanese courts.[122]

## 7
## CONCLUSION

Since no specific legal rules govern the termination disputes between manufacturers and distributors, court decisions have constituted the main source of law. Japanese case law and legal doctrine are not univocal, but in most cases the Japanese courts apply concepts such

115 Haley indicates that the actions filed for provisional relief and civil execution outnumber the ordinary civil suits. See J.O.Haley (1991), o. c., p. 118–119. Proceedings for provisional dispositions are commonly sought in intellectual property cases involving alleged infringements of patents and trademarks and in proceedings on wrongful dismissal when the employee wants the employer to continue to pay his wages temporarily.

116 Between 1980 and 1987 in only nine cases did distributors apply for an injunction before the Tokyo District Court to supply the goods. In only four cases was this granted. See H.Nakata (1994), o. c., p. 68–69.

117 See Kenji Iwaki, Noboru Kashiwagi, Kenji Kawagoe and Kōji Shindō (1995), *'Kakaku hakai genshōka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction), 561 *New Business Law* 29–31.

118 See K.Kawagoe (1995), Ibid, p. 31.

119 *See the Jeans case, 1490 Hanrei Jihō* 111 (Osaka District Court, 21 June 1993).

120 See J.Davis (1996), o. c., p. 291.

as 'unavoidable reasons' and 'breakdown of the relationship of trust', which provides them with much flexibility.

First, by applying these concepts Japanese courts seem to pay less attention to the contents of the underlying formal contractual terms when considering all the relevant circumstances for the decision. Compared to the Dutch courts the Japanese courts do not attach much weight to the provisions setting forth the contract period and the period of prior notice required to terminate the contract. They make almost no distinction between contracts concluded for a fixed period and those concluded for an indeterminate period.

Accordingly, there seems to be a Japanese judicial practice of employing a discretionary method of interpreting the parties' intent as set out in the contract. While relying on their competence to interpret contracts in these termination disputes they have often interpreted the contract terms to mean something different from what the parties clearly spelled out in the contract. Generally speaking this judicial practice may be a characteristic of Japanese contract law.[123]

Furthermore, another important characteristic is that in cases of termination, Japanese courts do sometimes not distinguish the differences between distribution agreements and other continuing commercial contracts within Japan, neither do legal scholars. Both often collectively call these contracts 'continuing trade contracts' or 'continuing supply contracts'. They argue that the same principles should apply in all continuing commercial relationships.

Second, by applying these concepts Japanese courts often go further than the Dutch courts in requiring a good reason for the termination of a distribution agreement. For example, Japanese courts have repeatedly refused to allow unilateral refusal to renew distribution agreements without unavoidable reasons. These judicially created rules that prevent unilateral termination of distribution agreements notwithstanding the lack of contractual commitments to continue dealing may reflect a difference in the degree of trust within the commercial relationship between the suppliers and the distributors between both countries.

Termination disputes in Japan may illustrate the way in which commercial custom and commercial expectations both inform and are informed by judicial decision making, and therefore, within Japan there might be a stronger reliance on trust and may be even a stronger moral connotation upon continuing a commercial contract. This has resulted in the strong 'bias towards renewal' which has been confirmed in Japan by some influential court decisions.

However, some Japanese legal scholars argue that the current stagnation of the economy and the resulting inevitability of more unilateral terminations of contracts with distributors

121 See E.Blankenburg and F.Bruinsma (1994), o. c., p. 42.

122 In chapter 5 more is explained about these summary procedures.

123 See Zentarō Kitagawa (1997), 'Use and Non-Use of Contracts in Japanese Business Relations: A Comparative Analysis,' in: H.Baum (ed), *Japan: Economic Success and Legal System,* p. 161– 162.

and the current efforts toward deregulation requires further emphasis on the principle of freedom of contract and has weakened the notion of the protection of the weaker party. This may be illustrated by some recent influential court decisions in Japan.

Finally, it needs to be noted that there are many formal barriers to litigation for distributors in Japan. There is no speedy injunction procedure as in the Netherlands, which leads to the conclusion that Dutch distributors have more possibilities to take on their suppliers than their Japanese counterparts when distribution agreements have been terminated.

# 3
# Japanese Anti-trust Law and the Unilateral Termination of Distribution Agreements

## 1
## INTRODUCTION

Within industries where manufacturers enjoy a great deal of market control over their distributors with their own marketing methods, Japanese anti-trust law can have an important influence. The reason for the intervention of the anti-trust law is the potential unfair exercise of such market control by the manufacturer. It has an important function to protect the many small businesses in Japan against unfair trade restrictions by manufacturers which may impede them in freely conducting their business.[1] The Anti-monopoly Act can function indirectly to protect the distributor.

First, the Japanese Anti-monopoly Act places some restrictions on the content of a distributorship agreement and on the way in which distribution channels are formed by leading manufacturers. It can have an important impact upon the way termination clauses in the standard-form distribution contracts are drafted. Manufacturers have often amended distribution contracts in order not to violate the Act.

Second, if leading manufacturers unilaterally cancel their distributorship agreements Japanese anti-trust law can have an important indirect bearing upon subsequent termination disputes. This applies to cases where manufacturers want to maintain control over distribution channels and cancel contracts with distributors which do not abide by their trade policies, which in itself violates the Anti-monopoly Act.[2]

In response to a termination of the distribution agreement distributors can file a complaint with the Japanese Fair Trade Commission (FTC) and/or invoke the Anti-monopoly Act in a private lawsuit before the civil courts. In addition to invoking general principles of contract law, such as the principle of good faith, distributors can claim before the civil courts that the termination itself, or the clauses justifying it, are in violation of the Anti-monopoly Act and are therefore invalid. Furthermore, they can claim that the refusal to continue trading constitutes a violation of the Act.

This requires an explanation of what kinds of terminations of distribution agreements or refusals to deal may constitute such a violation. At the outset, this can be very difficult since manufacturers seldom justify a termination of a distri bution agreement by pointing

to non-compliance on the part of the distributor with an obviously forbidden trade practice such as resale price maintenance.

First, a description will be given of the relevant Articles of the Anti-monopoly Act and the related special Guidelines issued by the FTC. This will be followed by a brief study of the public law enforcement of Japanese anti-trust law in general. Subsequently, I will describe the private law enforcement of relevant anti-trust law before the civil courts and finally the effectiveness of an (additional) complaint by a distributor with the FTC. There exists a subtle interrelationship between contract law and anti-trust law in relation to the unilateral termination of distribution agreements. There has been a great deal of controversy since the enactment of the Anti-monopoly Act in 1947 concerning its private law influence. For illustrative purposes a brief comparison will be made with the applicable EU and Dutch anti-trust law.

## 2
## SUBSTANTIVE JAPANESE ANTI-TRUST LAW

### 2.1
### The Japanese Anti-monopoly Act

#### *General Information about the Act*

The Japanese Anti-monopoly Act was enacted in 1947 during the occupation of Japan by the allied forces following World War II. This new policy consisted of specific measures including the dissolution of *Zaibatsu,* the de-concentration of economic power and the disbanding of private control bodies. It was intended to create an institutional structure in which private firms would have equal opportunities to exert their capabilities and engage in free competition. The implementation of the new Act has not always been a smooth process. In subsequent years the Act has been amended several times and the development of the law has been marked by considerable fluctuation in the rigidity in its enforcement.[3]

As the Japanese legal scholar Kenji Kawagoe points out, the Anti-monopoly Act is in fact a law which differs a great deal from other Japanese laws. More than on the companies themselves the Act focuses on the market. Whereas other laws such as the Civil and Commercial Code focus their attention on circumstances on a micro-level, this law

1 Hiroshi Iyori (1997), *Dokusen kinshi seisaku to dokusen kinshihō* (Anti-monopoly Policy and the Antimonopoly Act), p. 66–72.

2 Kenji Kawagoe (1988), *Keizokuteki torihiki keiyaku no shūryō* (The Termination of Continuing Trade Contracts) 18 *New Business Law (Bekkan)* (Separate Volume), p. 76.

3 See K.Kawagoe (1997), *Dokusen kinshihō* (The Anti-monopoly Act), p. 5–7 and Mitsuo Matsushita (1993), *International Trade and Anti-trust Law in Japan,* p. 139.

primarily focuses on macro-level conditions. Therefore, from the point of view of other laws, which are made out of rights and obligations, it is indeed an exceptional law. Kawagoe also refers to the fact that not much is known about the degree to which the law has penetrated Japanese society. It receives much media coverage and many people know of its existence but they are usually not familiar with its contents. In addition, this law distinguishes itself from other laws in that the provisions of the Act are much more difficult to understand than the provisions of other laws. A special study is required if one wants to know what constitutes a violation of the Act. Finally, another special characteristic of this law is that the rigidity of its enforcement differs as far as various people and times are concerned.[4]

### *Relevant Code Provisions*

The Japanese Anti-monopoly Act covers three main areas: private monopolisation, inreasonable restraints of trade and unfair trade practices. The area of most relevance for termination disputes in relation to distribution agreements is the prohibition of 'unfair trade practices' under Article 19 of the Act.[5] In some cases the termination of the distribution agreement, or the clauses justifying it, may constitute an 'unfair trade practice'. The purpose of prohibiting these practices is to protect small businesses such as small distributors when there is a great disparity in the bargaining power between them and large enterprises.

In Article 2(9) these unfair trade practices are defined.[6] It is important to note that one of the requirements for an unfair trade practice is that the conduct 'tends' to impede fair

4 See K.Kawagoe (1997), o. c., p. 2–4.

5 This Article reads: 'No entrepreneur shall employ unfair trade practices'.

6 The two relevant clauses in this Article read: 'The term 'unfair trade practices' as used in this Act shall mean any act coming under any of the following items, which tends to impede fair competition and which is designated by the Fair Trade Commission as such:

(i) Unjustly discriminating against other entrepreneurs;…

(iv) Dealing with another party on such terms as will unjustly restrict the business activities of the said party'.

7 For an activity to qualify as an unfair trade practice, one of the requirements is also that the FTC must have designated the activity as an unfair trade practice. The FTC's 'general designations' *(ippan shitei)* specify certain broad practices coming under the purview of Article 9(2) and apply to all fields of trade.

8 No. 12 of the general designation reads: 'Supplying a commodity to the other party who purchases the said commodity from oneself while imposing, without proper justification, one of the restrictive terms specified below:

(i) Causing the said party to maintain the sales price of the commodity that one has determined, or otherwise restricting the said party's free decision on sales price of the commodity; or

(ii) Having the said party cause an entrepreneur who purchases the commodity from the said party

competition. This means that as long as there is a possibility for such impediment, the requirement is satisfied.

The same article also delegates authority to the Fair Trade Commission to designate unfair trade practices within the framework of the law. In order to give more guidance on what constitutes an unfair trade practice the most recent general designation on unfair trade practices was promulgated in 1982, replacing the earlier general designation of 1953.[7] The following provisions have proven to be the most important for distributors in termination disputes:

Article 2(9)iv of the Act provides that trading with another party on such conditions as will unjustly restrict the business activities of such party is an unfair trade practice.

First, under this heading the FTC announced in the 1982 general designation under No. 12 that resale price maintenance without good reason is prohibited.[8] This means that a manufacturer may not sell a commodity to distributors on condition that they observe the resale price indicated by the manufacturer. However, this rule only applies if there exists a binding obligation that the reselling parties must observe the price levels set by the manufacturer. A mere 'suggested' or 'recommended' price does not amount to resale price maintenance as distributors are under no contractual or de facto obligation to observe it.

Second, the FTC announced in the same designation under No. 13 that dealings on unjust restrictive terms are prohibited.[9] No. 13 could be applicable to customer restriction and territorial restriction. As regards customer restriction the FTC decisions have consistently made it illegal for a manufacturer to demand that its customers suspend shipments to, or refuse to deal with, retailers who sell below the manufacturer's suggested resale prices. However, apart from customer restriction for the purpose of maintaining resale prices such restriction is not held to be an illegal conduct in principle.

Finally, it is also important to point to Article 2(9)i which provides that unreasonable discrimination exercised by an enterprise is an unfair trade practice. Under this heading the FTC announced in the general designation that an undue individual refusal to deal with a particular entrepreneur (No. 2)[10] constitutes an unfair trade practice. This applies when such a refusal is used to achieve an illegal purpose such as resale price maintenance.

Generally speaking, no clear distinction is made in Japanese anti-trust law between vertical trade restraints as set out in No. 12 and 13 and such an individual refusal to deal as set out in No. 2. A termination of a contract or a halt in supplies by a manufacturer, which supports resale price maintenance or a dealing on unjust restrictive terms, may also fall under No. 2 of the general designation.[11]

In 1991 the FTC has clarified these rules within the general designations by issuing special guidelines.

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to maintain the sales price of the commodity that one has determined, or otherwise causing said party to restrict the said entrepreneur's free decision on sales price of the commodity'. (Translation, H.Iyori and A.Uesugi (1983), *The Anti-monopoly Laws of Japan,* p. 265–270).

## 2.2
## The Guidelines concerning Distribution Systems and Business Practices of 1991

### *Introduction*

At the end of the 1980s the us increasingly exerted pressure for a stronger enforcement of the Japanese Anti-monopoly Act. This US pressure was illustrated by the 1989 Structural Impediment Initiative (SII) talks between the two countries. The US negotiators had claimed that many trade practices in Japan constituted invisible trade barriers which precluded new market entrants from establishing links in the distribution sectors of the Japanese economy. They argued that many unfair competition devices such as resale price maintenance were maintained. In response to these claims a private study group established by the FTC prepared a report[12] in which possible violations of the Anti-monopoly Act were set out and which prepared the way for the introduction of new very influential Guidelines.

Partly in response to US pressure, in July 1991 the FTC introduced Guidelines concerning distribution systems and business practices, in order to increase compliance with the Anti-monopoly Act.[13] The official purpose of the introduction of the Guidelines was to clarify which trade practices in distribution violate the Act and which practices do not. In this way businesses could take preventive measures so as not to violate the Act.[14] According to Japanese legal scholar Akinori Uesugi these Guidelines indicate for the first time the FTC interpretation of the related items of unfair trade practices systematically based on case law as well as FTC decisions rendered so far, and analysis of the business practices of Japanese companies.[15]

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9 No. 13 of the general designation reads: 'Other than any act coming under the preceding two paragraphs, dealing with the other party on conditions which unjustly restrict any transaction between the said party and his transacting party or other business activities of the said party'. (Translation, Ibid.).

10 No. 2 of the general designation reads: 'Unjustly refusing to deal, or restricting the quantity or substance of a commodity or service involved in the transaction with a certain entrepreneur, or causing another entrepreneur to take any act which comes under one of these categories'. (Translation. Ibid.).

11 See Masahiro Murakami (1997), *Dokusen kinshihō kenkyū* (A Study of the Anti-monopoly Act), p. 45–46.

12 Report of 21 June 1990, outlined in 453 *New Business Law* 9, (1990).

13 The Executive Office of the Fair Trade Commission, *Ryūtsū torihiki kankō ni kansuru dokusen kinshihō jō no shishin* (The Anti-monopoly Act Guidelines concerning Distribution Systems and Business Practices), (11 July 1991). In Japanese, but the English version is also available at the FTC. In addition a full translation can be seen as Appendix H of H.Iyori and A.Uesugi (1994), *The Anti-monopoly Laws and Policies of Japan,* p. 493. For an explanation of the Guidelines see A.Yamada, M.Ōkuma and N.Narasaki (1993), *Ryūtsū torihiki kankō ni kansuru dokusen kinshihō gaidorain* (The Anti-monopoly Act Guidelines concerning Distribution Systems and Business Practices).

14 See A.Yamada, M.Ōkuma and N.Narasaki (1993), Ibid., p. 9.

Generally speaking, the FTC issues many guidelines in which it clarifies its viewpoint on difficult issues.[16] They are comparable to circulars used in tax law and share the advantage of enhancing to some degree the predictability of the law.

Although the Guidelines are presented as an informal expression of the viewpoint of the FTC, which cannot bind the courts, in actual practice they exert a great deal of influence. This is illustrated by the fact that many Japanese companies have taken precautionary measures in order not to violate the Guidelines. Furthermore, in the explanatory notes to a decision the FTC bureaucrats take more care to ensure that their decision matches what is written in the Guidelines than that it matches what is written in the Anti-monopoly Act. Many legal scholars and civil court judges also tend to use the expressions set out in the Guidelines.[17] It is therefore difficult to draw conclusions about the exact legal position of these Guidelines. This may illustrate that the distinction in Japan between formal and informal law is vague.[18]

### *Relevant Provisions*

First, of much importance for distributors who want to invoke anti-trust law after the contract has been cancelled, is that which the Guidelines state in relation to No. 12 of the general designation on resale price maintenance. They stipulate that resale prices are considered to be restricted when a written or oral agreement between a manufacturer and its distributors or any artificial means used by the manufacturer, causes distributors to sell at the price indicated by the manufacturer. One of these artificial means may consist of curtailments of shipments or a notification or suggestion to that effect if sales are not made at the manufacturer's indicated price.[19]

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15 See Akinori Uesugi (1999), 'Unfair Business Practices', in: Zentarō Kitagawa (ed), *Doing Business in Japan* Vol. 9, Chapter 6, p. 7.

16 See Tadashi Shiraishi (1997), *Dokkinhō kōgi* (Lessons in the Anti-monopoly Act), p. 138.

17 T.Shiraishi (1997), o. c., p. 138–139.

18 According to legal scholar Tadashi Shiraishi these Guidelines are treated just like 'formal' laws. See T.Shiraishi (1997), o. c., p. 138. However, he may thereby have failed to notice that 'informal' laws (the Guidelines) may have more influence than 'formal' laws such as the Anti-monopoly Act.

19 Part II, Chapter 2, Section 1 and 2 of the Guidelines, See A.Yamada, M.Ōkuma and N.Narasaki (1993), Ibid., p. 136–155.

20 They state: 'In case the manufacturer's prohibition on sales among distributors is carried out in order to prevent sales of its product to discounters, and if therefore, the price level of the product covered by the restriction is likely to be maintained, such prohibition is illegal'. Part II, Chapter 2, Section 4 of the Guidelines, Ibid., p. 178–185.

21 They state: 'In case a manufacturer pressurises wholesalers not to sell to retailers on account of their discounting or when a manufacturer ceases to supply its direct distributors because they were selling at a discount, and if therefore, the price level of the product is likely to be maintained, such acts are illegal'. Part II, Chapter 2, Section 4 of the Guidelines, Ibid., p. 178–185.

Second, also important is what the Guidelines stipulate in relation to No. 13 of the general designation, which prohibits dealings on unjust restrictive terms. They provide rules on restrictions on customers, sales territory, sales methods and handling of competing goods. The provisions regarding the restriction on customers and sales methods have proven to be the most important for distributors in termination disputes.

As for customer restriction the Guidelines declare such restriction illegal if, as the result of such conduct, the price level of the product covered by the restriction is likely to be maintained. For example, this concerns the prohibition on sales among distributors[20] and the prohibition on sales to discounters.[21] However, the Guidelines do not clarify to what extent the price level must be maintained in order to make such types of conduct illegal.[22] As regards the restrictions on the sales methods of retailers, the Guidelines first state that such restrictions would not violate the Act if they were necessary or helpful in ensuring proper sales of the product, product safety, quality control or maintenance of goodwill and are imposed in a similar way on all other trading partners. However, such restrictions are regarded as unfair trade practices if they are used as a means to restrict the retailer's sales price, customers, sales territory or handling of competing goods.[23]

Finally, as for No. 2 of the general designation on individual refusals to deal, the Guidelines describe some concrete examples of such refusals which could fall under this item. They first stipulate that in principle companies are free to trade with the company they want. However, in exceptional cases when a refusal to trade is a means to secure the efficacy of an act which violates the Anti-monopoly Act, it is illegal. The same applies when the refusal to trade is a means to achieve an unjust purpose such as excluding competitors from the market.[24]

It is important to note that this applies both in cases where trade is rejected with already existing trading partners or where trade is rejected with a company which wants to

22 M.Murakami (1997), o. c., p. 45, 125; H.Iyori (1997), o. c., p. 641. These legal scholars argue that in general the Guidelines leave many questions unanswered. See M.Murakami (1997), o. c., p. 46; H. Iyori (1997), o. c., p. 651.

23 Part II, Chapter 2, Section 5 of the Guidelines, see A.Yamada, M.Ōkuma and N.Narasaki (1993), o. c.,p. 185–189.

24 Part I, Chapter 3, Section 1–3 of the Guidelines, see A.Yamada, M.Ōkuma and N.Narasaki (1993), o. c.,p. 70–77.

25 Ibid., p. 71.

26 Ibid.

27 H.Iyori (1997), o. c., p. 633, 657.

28 In general, with the new Act Dutch anti-trust law has almost completely moved towards the approach in EU anti-trust law. It is only applicable when competition is affected or restricted within the Netherlands.

29 In relation to vertical restrictions the Guidelines stipulate that there is a violation 'when it is likely that the restrictions lead to price stability', which goes further than EU anti-trust law. Formally, the

commence trading with the said company.[25] It is further argued in the explanatory notes that although many continuing trade relationships are concluded for a specified duration with automatic renewal clauses, a refusal to trade based solely on the non-renewal of the contract, does not necessarily mean that such a refusal cannot violate the Anti-monopoly Act.[26]

## 2.3
## A Brief Comparison with EU and Dutch Substantive Anti-trust Law

Japanese anti-trust law as it applies to vertical restrictions within the distribution sector is not much different from equivalent EU anti-trust law.[27] Resale price maintenance and many other vertical restrictions are also prohibited in EU anti-trust law. Since the new Dutch Competition Act of 1998 now follows the same approach of EU law on vertical restrictions it is also not so different from national Dutch anti-trust law either.[28]

However, formally the Japanese Guidelines are more rigid in relation to the prohibition of resale price maintenance and other vertical restrictions than EU anti-trust law.[29] It must be noted, though, that the Guidelines still leave many questions open and provide less clear rules on vertical restrictions than EU anti-trust law. In relation to the restrictions on the distributors' customers or sales methods, there have been almost no formal decisions of the FTC or the courts in order to answer these questions.[30] By contrast, there are many decisions by the Community Courts and the Commission on this issue. For example, in Japan there is not such detailed case law on selective distribution agreements as there is in the EU where over the years many decisions have been delivered on the issue whether the restrictions on retailers as stipulated within such agreements may contravene EU anti-trust law.

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prohibition on resale price maintenance is also more rigid. In the Guidelines not only is resale price maintenance forbidden when there is some sort of 'agreement' but also when 'any artificial means used by the manufacturer' causes distributors to sell at the price indicated by the manufacturer. See H.Iyori (1997), o. c., p. 626–641.

30 M.Murakami (1997), o. c., p. 44–46; p. 125; H.Iyori (1997), o. c., p. 651. However, in relation to restrictions on the distributor's sales methods and customers recent decisions of the Tokyo High Court and the Supreme Court have provided more clarity on this issue. These will be briefly described in section 3.4 and in much more detail as a case-study in the next chapter.

31 It must be noted that current EU law on vertical restraints will be reformed on June 2000. For example, there will be a single umbrella Block Exemption Regulation covering all forms of vertical restraints including selective distribution agreements.

32 H.Iyori, (1997), p. 613–614, 657. Hiroshi Iyori also refers to the fact that in comparison with the powerful ministries regulating industry the influence of the FTC is weak.

33 Ibid., p. 613–616.

34 Ibid., p. 658.

Furthermore, the formal notification system in EU anti-trust law with its resulting block exemptions in relation to various kinds of distribution agreements provide more knowledge about what kind of restrictions are in violation of anti-trust law.[31]

One reason may be that in general compared to EU anti-trust law the enforcement of anti-trust law by the FTC has been weaker and more informal. Differences with EU anti-trust law are mainly found in enforcement.[32] The more informal approach in Japan is evidenced by the smaller number of formal decisions by the FTC and the Tokyo High Court which can clarify difficult issues when compared to the decisions taken by the EU Commission and Community Courts.[33] Legal scholar Hiroshi Iyori explains this more informal approach, often referred to as 'administrative guidance', by Japanese tradition and the influence since the Meiji period (1868–1912) of the policy of giving priority to industry. In order to allow industry to catch up with the Western nations, sanctions such as huge fines were not imposed. However, he argues that when Japan caught up with the West in the 1970s such a justification for informal enforcement had lost its validity.[34]

## 3
## PUBLIC LAW ENFORCEMENT OF ANTI-TRUST LAW

### 3.1
### Fair Trade Commission

So far, the Anti-monopoly Act has been mainly enforced by the Fair Trade Commission (FTC) which is authorised to investigate suspected violations. Although it administratively belongs to the jurisdiction of the Prime Minister it is an ExtraMinisterial Agency attached to the Prime Minister's office composed of a Chairman and four Commissioners. The Chairman and the Commissioners are appointed by the Prime Minister for five-year terms with the consent of both Houses of the Diet from individuals who are considered experts in the law and economics. The General Secretariat is attached to the Commission and executes the day-to-day operations.[35] The staff consists of over 500 people. By means of a 1996 revision to the Act the FTC has been reorganised and strengthened. It has been made more efficient and the new General Secretariat is now composed, under its Secretary General, of a Secretariat (composed of three divisions), an Economic Affairs Bureau (four divisions and one department) and an Investigation Bureau (four divisions and one department). In addition, it has five Hearing Examiners, who hold hearing procedures as commissioned by the FTC.

The FTC is an independent administrative agency and has the power to exercise a quasi-legislative and quasi-judicial power in addition to its administrative power. As a quasi-legislative power the FTC has rule making competence to designate commodities for which

35 When one refers to the FTC, in most cases in reality one means the General Secretariat The activities and the role of the Commissioners, including the Chairman, is not entirely clear. See T. Shiraishi (1997), o. c., p. 131.

resale price maintenance is permissible and to define unfair trade practices. Furthermore, it can establish the procedure for handling cases brought before it and it determines the form of complaint required to be filed with the FTC.

## 3.2
## Procedures before the FTC

As a quasi-judicial power the Anti-monopoly Act provides the procedures to be followed by the FTC when handling cases it has found to violate the Act (see Graph 3–1). Preliminary evidence of a possible violation of the Act, which prompts the FTC to initiate an investigation, can be classified under the following three types:

1 Complaint from the public (Article 45(1));
2 Detection by the FTC's own authority (Article 45(4));
3 Notification by the Public Prosecutor General (Article 74).

Complaints from the public play the most important role. Any person may request that the FTC institutes an investigation into any facts suspected of being in viola tion of the Act. If the FTC initiates an investigation this can be done on a voluntary basis when the co-operation of the firms investigated can be obtained, but sometimes this is inadequate and a compulsory investigation is conducted. The FTC can undertake an investigation by designating investigators to enter the premises of companies and to force these companies to submit necessary reports, information or data or even to order persons to appear to give evidence on specific details.

When the FTC concludes that alleged facts have violated the Antimonopoly Act it can recommend that measures be taken to eliminate such acts. Any person who has received such a recommendation must notify the FTC in writing without delay as to whether it will accept the recommendation. When it is accepted and the respondent voluntarily agrees to take corrective measures the FTC can issue a recommendation decision *(kankoku shinketsu)*[36] without initiating hearing procedures.

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36 See Article 48 of the Anti-monopoly Act. These are by far the most frequent decisions by the FTC. In a report of the FTC from August 7, 1996 in which all the FTC decisions since the enactment of the Anti-monopoly Act of 1947 are reported, among the total amount of 1002 decisions 776 (77.4%) were recommendation decisions.

37 In actual practice these procedures are only conducted by three Hearing Examiners. These consist of two officials of the FTC and one court judge. See T.Shiraishi (1997), o. c., p. 132.

38 See Article 53(3) of the Anti-monopoly Act. In the annual report of the FTC for fiscal year 1996 among 1002 decisions 115 decisions were consent decisions (11.5%).

39 See Article 54 of the Anti-monopoly Act. In general, the number of hearing decisions is very limited. In the FTC report among 1002 decisions 99 were hearing decisions (9.9%).

When the violator does not accept the recommendation hearing procedures are initiated. These procedures are similar to court proceedings in that the Commission or hearing examiners conduct them.[37] The investigators try to prove the violation of the act while the respondent (the suspected violator) counters this attempt. However, if in the middle of hearing procedures the respondent submits a written statement in which the facts in the application of the law as stated in the complaint are accepted and measures are proposed to eliminate the violation the FTC can issue a consent decision *(dōi shinketsu)*.[38] In the event that hearing procedures are completed without such consent decision the FTC issues a hearing decision *(seishiki shinketsu)*.[39] Depending upon the nature of the violation the content of a decision may take various forms. The FTC has the authority to take out an injunction against a violation which can take the form of a cease-and-desist order or affirmative relief. Furthermore, the FTC can impose an administrative fine.

Those who are dissatisfied with a decision of the FTC can file a lawsuit to quash the decision. The Tokyo High Court has exclusive jurisdiction to review a decision of the FTC. The scope of judicial review of an FTC decision is whether it is supported by substantial evidence or whether it is not contrary to the Constitution or other laws.[40] Finally, the Tokyo High Court decision can be appealed before the Supreme Court.

However, it seldom goes that far. In most cases the FTC works on an informal basis and does not even issue a recommendation decision.[41] In the event that the FTC concludes that alleged acts may violate the Act it usually takes informal measures such as warnings *(keikoku)* or cautions *(chūi)*.[42]

These informal warnings or cautions are issued typically in cases where the violation is minor.[43]

The FTC's informal approach is also evidenced by the fact that it usually works on the basis of prior consultation.[44] The Guidelines of 1991 have also established a prior consultation system.[45] They provide that in general advance consultation can be done orally as before, but they also enable parties to consult in advance in writing which means that they can send their contracts for approval. In such cases the FTC also replies in writing. When it concerns distribution contracts one party to the contract or both parties together may conduct prior consultation. If one party requests approval the FTC may hear the other party if it deems this necessary.

The FTC may declare that the act or contract in question does not violate the Anti-monopoly Act and it will notify that it will not take any legal measures. However, it can set conditions or time limits with the reply and may revoke the initial reply when circumstances have changed. The Guidelines also state that, provided there are no obstacles, the FTC will make its reply public. Recently the FTC has become more active in so doing.[46]

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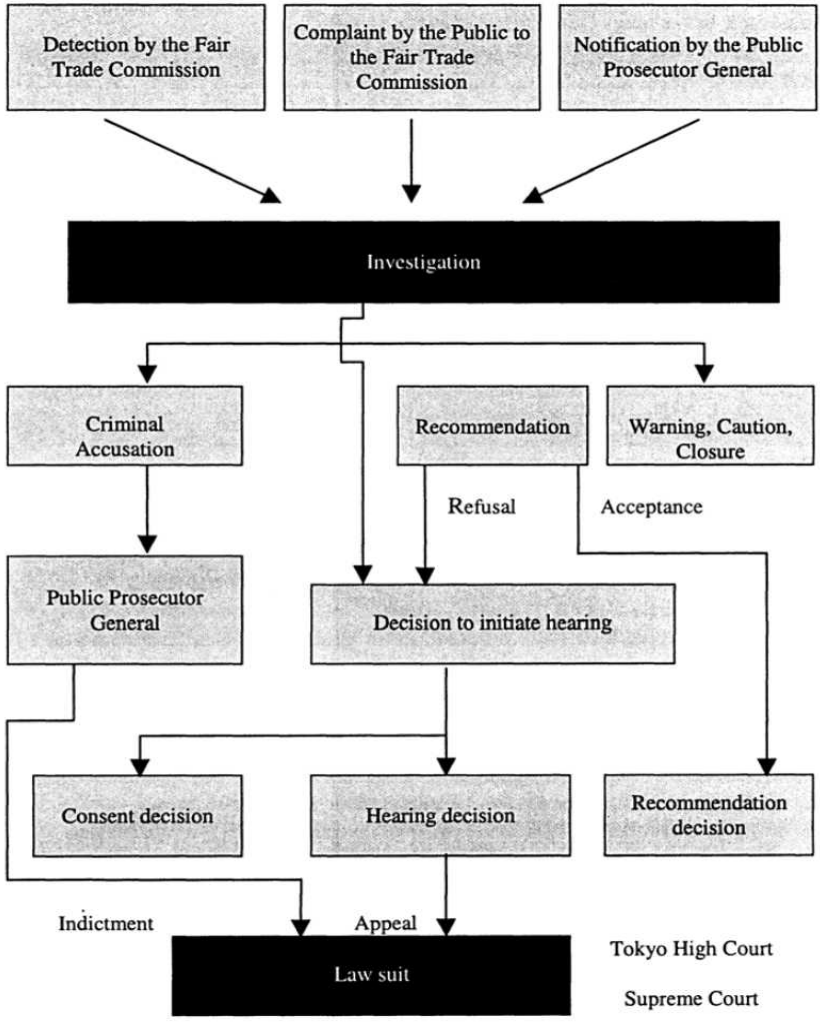
40 Generally speaking, so far since the enactment of the Anti-monopoly Act in 1947, in only around 30 cases has the Tokyo High Court decided upon a decision by the FTC. See H.Iyori (1997), o. c., p. 616.

Graph 3–1: Procedures before the FTC




Source: Homepage of the FTC: http://wwwjftc.admix.go.jp.

In actual practice this advance consultation system has had a great deal of influence. So far Japanese manufacturers have often submitted their contracts for prior approval since they are afraid of the negative consequences in the event that these contracts may violate the Act. They would rather take precautionary measures than risk a loss of reputation, time and money.[47]

## 4
## PRIVATE LAW ENFORCEMENT OF ANTI-TRUST LAW

### 4.1
### Introduction

Generally speaking, the relationship between the provisions of the Anti-monopoly Act and the Civil Code is unclear. The Act does not contain any provisions on the private law influence of a violation. The enforcement of the Act has been entrusted to the administration (FTC) and there are no provisions stipulating whether any conduct in violation of the Act is valid, void or voidable before civil courts. This means that it is very difficult to draw any conclusions.

Nevertheless, increasingly the civil courts have been asked to provide help against anti-competitive acts in Japan. In fact, there has been a great deal of controversy concerning the private law enforcement of a violation of anti-trust law in Japanese case law. First, there are doubts whether the courts have sufficient expertise to judge on anti-trust issues. Many Japanese legal scholars argue that the necessary expertise on anti-trust law issues is usually lacking among lawyers and judges.[48] For example, the Japanese National Bar Examination

41 See T.Shiraishi (1997), o. c., p. 139–140. See also, M.Matsushita, (1993) o. c., p. 141.

42 According to the annual report of the FTC for fiscal year 1998, it issued 62 cautions and 17 warnings. By contrast, there were 27 recommendation decisions which led to only 3 commencements of hearing procedures.

43 See T.Shiraishi (1997), o. c., p. 139–140. Tadashi Shiraishi contends that there are indications that the FTC may also issue these warnings when it is not completely sure whether there has been a violation or not. He also holds that perhaps the FTC is cautious about issuing recommendations because there is always the risk that respondents reject the recommendation which leads to hearing procedures. This would make the investigators of the FTC more busy and less able to handle other cases.

44 This is not so very different, though, from Commission practice which also mainly works with so-called 'comfort letters' in which it grants exemption from a violation of EU anti-trust law.

45 See A.Yamada, M.Ōkuma and N.Narasaki (1993), o. c., p. 296–302.

46 T.Shiraishi (1997), o. c., p. 22, 93. These replies are reported in *Kōsei Torihiki*, the journal published by the FTC. According to legal scholar Masahiro Murakami these replies do not express a judgement of the FTC. It remains an 'informal' measure. See M.Murakami (1997), o. c., p. 128.

47 T.Shiraishi (1997), o. c., p. 138.

does not include anti-trust issues. This may be most evident in injunction proceedings where usually young and inexperienced judges are hesitant to deliver decisions on difficult legal issues such as anti-trust law.

Another problem is that the civil courts do not have the investigative powers of the FTC. They are dependent on the evidence presented to them by both parties.[49] A distributor may demand information from the FTC directly but Article 69 of the Anti-monopoly Act stipulates that victims of a violation only have the right to demand information about the case from the FTC after it has decided to commence a hearing procedure which is not common. Also civil court judges may ask for information from the FTC but have so far rarely done so.

Furthermore, the fact that an appeal of an FTC decision lies exclusively in a special section of the Tokyo High Court is exceptional in Japanese jurisprudence and may reflect the importance attached to the expertise of the FTC in anti-trust cases. This may provide an argument against the enforcement of anti-trust law by other civil courts.[50] For these reasons some court decisions have assumed that the application and the enforcement of the provisions of the Anti-monopoly Act is in the exclusive domain of the FTC. However, currently the majority of civil court judges agree that anti-trust issues must also be resolved before their courts because the enforcement by the FTC alone is not sufficient. Nevertheless, there is still no uniformity regarding the exact private law consequences of a violation of the Act.

So far the number of termination disputes in which Japanese anti-trust law has been invoked before the civil courts by one of the contracting parties has been limited, but compared to other kinds of civil disputes in which anti-trust law has been invoked, they comprise a majority. In most cases litigation was commenced by trading partners of the company accused of violating the Act. It is interesting to note that until 1997 out of a total of 64 cases in which anti-trust issues were invoked before the civil courts, 15 cases (a majority) concerned distributors who brought an action after the distribution agreement had been cancelled by a manufacturer.[51]

48 Kazuhiko Bandō (1998), *'Fukōsei na kyōsō kōi ni taisuru minjiteki kyūsai seido ni kansuru shuyō ronten —Kigyō hōsei kenkyūkai hōkokusho o sozai ni shite'* (Main Issues in relation to the Civil Remedy System in respect to Unfair Competition Acts—Based on the Report of the Research Committee on Business Law Systems), 644 *New Business Law* 16.

49 Minjiteki Kyūsai Seido Kenkyūkai (The Research Committee on the Civil Remedy System) and Mitsuo Matsushita (eds.) (1997), *'Fukōsei na kyōsō kōi to minjiteki kyūsai'* (Civil Remedy and Unfair Competition Acts), *New Business Law (Bekkan)* (Separate Volume), No. 43, p. 88.

50 See Christopher Heath (1995), 'Burgerliches Recht, Wettbewerbsrecht und Kartellrecht in Japan', *Wirtschaft und Wettbewerb* 2 1995, p. 100.

### 4.2
### Claim for Specific Performance

In most cases distributors have claimed specific performance of the contract or substitute damages,[52] contending that the manufacturer breached contractual terms because it did not supply, although the contract had remained valid. They claimed that the cancellation, or the clause justifying it, violated the Anti-monopoly Act and was therefore invalid.[53] Usually the demand for specific performance was preceded by a claim demanding legal confirmation that they still had the right to receive the supplies. Such claims for a confirmation of legal rights and a claim for specific performance have usually occurred in main suits and sometimes in injunction procedures. Whether such claims of a distributor can be successful depends on a number of factors:

Firstly, the court must conclude that the termination, or the contract provision justifying it, has violated the Anti-monopoly Act. Initially, the courts usually held that there had been no violation of the Act. Without success, distributors had invoked the illegality of a price-fixing clause,[54] a non-competition clause[55] and a clause restricting the sales territory,[56] in order to deny a valid cancellation of the contract. Suppliers had justified the termination with the non-compliance of the distributor as regards such clauses.

However, even if the court concludes that the Act might have been violated it still has to deny the enforceability of such a contract and argue that the termination, or the clause justifying it, is void. This depends on the way the court responds to the general question of the enforceability of contracts in violation of the Anti-monopoly Act. Cases are divided on this issue. In some cases the courts argue that a contract which is incompatible with the Act is thereby invalid and unenforceable. In other cases contracts are held valid by the courts despite their illegality. One common approach of the courts takes an intermediate course. This course is reflected in a Supreme Court decision which ruled that a contract violated

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51 See p. 19 of the report entitled: *Chiteki zaisan no funsō shori ni kansuru chōsa kenkyū hōkokusho — Kyōsō kankyō seibi no tame no minjikyūsai seido no kentō* (A Report on the Resolution of Disputes on Intellectual Property—An Investigation into the Civil Remedy System for Adjusting the Competition Order) issued in May 1997 by the Chiteki Zaisan Kenkyūsho (Intellectual Property Research Centre), and the Nihon Kikai Rengōkai. A number of prominent professors headed by Mitsuo Matsushita drafted this report. Part of this report is also published in an article by Takuya Sekiguchi (1997), *'Dokusen kinshihō ihan kōi ni taisuru minjiteki kyūsai seido no kentō'* (A Study of the Civil Remedy System in relation to violations of the Anti-monopoly Act), 625 *New Business Law* 17–23. See also Kenji Kawagoe (1997) in: Nikkei Business, 3 November 1997.

52 This kind of claim for damages based on the non-performance of contract must be distinguished from the possibility to directly claim damages based on the general tort provision of Article 709 of the Civil Code.

53 According to the report, issued in May 1997 by the Intellectual Property Research Centre, these claims play an important role in the private law enforcement of the Anti-monopoly Act. See p. 37.

54 490 *Hanrei Jihō* 51 (Tokyo High Court, 25 May 1967).

55 862 *Hanrei Jihō* 87 (Osaka District Court, 27 January 1977) and 591 *Kinyū Shōji Hanrei* 43 (Kobe District Court, 11 December 1979).

Article 19 of the Anti-monopoly Act, and was therefore illegal. Nevertheless it refused to declare the contract void in principle, reasoning that the purpose of the Act did not call for such drastic measures with regard to contracts based on unfair trade practices. It did not consider the contract to be invalid for being contrary to public order and good morals.[57] In this approach such contracts are only void if they are deemed to be contrary to public order and good morals of Article 90 of the Civil Code.[58] However, generally speaking, the courts have so far rarely held that contracts concluded by the use of unfair trade practices contravene public order and good morals.

*Miyagi Family Club v. Nihon Columbia*

For example, one termination dispute involved a music record retailer, which had concluded distribution agreements with a record wholesaler and two record manufacturers. Five years into the agreement the retailer began to sell records to record rental shops, which started to appear in Japan and expanded rapidly. Without success, the wholesaler and the two manufacturers repeatedly urged the retailer not to sell records to rental shops. Eventually, all the suppliers terminated their agreements with the retailer, reasoning that the distributor had breached contract provisions. In response, the distributor filed a petition with the court seeking a provisional disposition to confirm its continuing rights under the distribution agreement and to oblige the suppliers to deliver the records on order. The retailer claimed that the refusal of supplies constituted a 'collaborative boycott to trade' which violated Nos. 1 and 13 of the general designation. The retailer based this claim, among other things, on an informal warning *(keikoku)* by the FTC on 15 December 1982 directed towards record manufacturers and warning against refusing to trade with retailers who delivered records to record rental shops.

The FTC had found out that in order to stop supplies to record rental shops all members of the Japanese Record Association had agreed to urge their retailers not to supply these shops, to stop deliveries to retailers who did not give in to this demand and to check their own sales routes by attaching secret codes to their products. This was likely to be in violation of the Anti-monopoly Act.[59]

However, in relation to any private law enforcement the court held: "…the cancellation might have violated the Anti-monopoly Act but in view of the reciprocal rights and duties in the contract and the breach of contract it does not mean that it goes against public order and good morals and is therefore invalid". The court rejected the injunction and validated

56 *Young Winners case,* 1132 *Hanrei Jihō* 152, (Nagoya District Court, 21 February 1984).

57 *Miyagawa K.K. v. Gifu Commercial & Industrial Credit Assoc.,* 856 *Hanrei Jihō* 3 (Supreme Court, 20 June 1977).

58 The very important compulsory provision of Article 90 of the Civil Code reads: 'A juristic act which has for its object such matters as are contrary to public policy or good morals is null and void'. (EHS translation p. 17).

the cancellation which it justified on contract law. The breach was serious enough to cause a 'breakdown of the parties' trust relationship'.[60] On appeal, both parties reached a settlement in court (wakai). According to legal scholar Kenji Kawagoe the reason for this decision in favour of the manufacturer was that the court gave more preference to civil law than to the Anti-monopoly Act.[61]

### 4.3 Claim for Damages

Acts of unfair business practices constitute torts.[62] First, Articles 25 and 26 of the Act enable the party who incurs damage from the violation to bring an action for damages before the Tokyo High Court. The plaintiff needs to prove the amount of damage and the causal link between the damage and the illegal conduct. He may recover without proving negligence or intentional conduct.

However, such action is only possible after the FTC has investigated a charge and delivered a decision. Only in two cases did distributors claim damages while directly invoking these provisions of the Anti-monopoly Act. In one case a non-competition clause imposed by a large Japanese manufacturer of pharmaceutical products on more than 3,000 retail drugstores was held to be illegal by the FTC in a recommendation decision.[63] The suspension of supplies, which was justified by a breach of this clause by a distributor, was therefore in violation of the Act.[64] While invoking Article 25, one of the retail drugstores sought to recover damages, which had been caused by the suspension of trade by the manufacturer. The dispute was eventually settled and the court issued a settlement judgement *(wakai)*. Both parties agreed to recommence trade and damages were awarded to the retailer to the amount of 200,000 Yen.[65] In a similar case a distributor had filed suit for damages before the Tokyo High Court but five years later withdrew it.[66]

Second, where there is no FTC decision regarding the illegal conduct, which may have caused damage to the distributor, the latter may also bring an action on the basis of Article 709 of the Civil Code, the general tort provision.[67] In these cases he must prove the illegality of the conduct which caused the injury. In two cases distributors have brought a tort suit against the manufacturer before the District Court but they have so far never proved successful.[68]

Generally speaking, so far in Japanese actual practice the private actions by claiming damages against manufacturers because they refused to trade or ceased trading do hardly

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59 *Kōsei Torihiki Tokuhō,* Vol. 545. (FTC Recommendation Decision, 15 December 1983).

60 *Miyagi Family Club K.K. v. Nihon Columbia K.K. et al.,* 1110 *Hanrei Jihō* 13 (Tokyo District Court, 29 March 1984).

61 See K.Kawagoe (1988), o. c., p. 78.

62 43 *Shinketsushū* 579 (Tokyo High Court, 31 May 1996).

63 *FTC v. Taishō Seiyaku K.K.*, 7 *Shinketsushū* 99 (FTC Recommendation Decision, 10 December 1955).

64 No. 11 of the former general designation of 1953, Article 7.

function at all.[69] Japanese procedural law constitutes a great barrier for such actions. It is therefore no exaggeration to say that a claim for damages by distributors against a manufacturer is hardly is an option for them.

Compared to the costs of litigation the award of damages is usually very limited. Since distributors are usually small and have little financial resources the incentives to file such suits are very small. There are also many other procedural barriers. For example, when distributors want to claim damages based on Articles 25 and 26 of the Act they have to wait for a decision by the FTC and it is difficult for them to obtain information from the FTC in order to gather sufficient evidence before the Tokyo High Court. This is because most decisions are recommendation decisions which are not based on a finding of a violation proven by evidence but solely on the respondent's agreement to accept the recommendation voluntarily.[70] Furthermore, when distributors want to bring an Article 709 tort claim, it proves to be very difficult for the litigants to respond sufficiently to the demand of the court to prove the causation, the damage and the amount of damage sustained.

On 15 May 1991 the FTC had issued measures to enable parties to request information from the FTC in order to collect evidence in tort proceedings but this is still not sufficient.[71]

## 4.4 Recent Cases in the 1990s

Although the numbers are still limited, recently for the first time the lower courts have started to declare unilateral terminations, or clauses justifying it, void, partly because of a violation of anti-trust law. Many of these disputes must be viewed against the background of a period of further discounting in Japan starting at the beginning of the 1990s in which in some industries leading manufacturers tried to maintain control over distribution

65 On 19 February 1958 both parties reached a settlement in court before the Tokyo High Court, 9 *Shinketsushū* 162.

66 This suit was filed in 1983 and was eventually withdrawn on 26 December 1988. Both parties reached a settlement in court in a related case before the Ōta District Court.

67 There has been some controversy as to whether a person injured by an act which may constitute an violation of the Act may bring a 709 tort claim, but some decisions support such a claim.

68 *Jeans case,* 1490 *Hanrei Jihō* 111 (Osaka District Court, 21 June 1993) and *Oppen cosmetics case,* 39 *Shinketsushū* 581 (Osaka District Court, 24 July 1992).

69 See Masahiro Murakami (1997), o. c., p. 85. In general the courts have rarely decided that a violation of the Anti-monopoly Act would constitute a basis for a tort claim under the Civil Code. Ramseyer claims that in actual practice this kind of private enforcement has almost been non-existent. See, J.M.Ramseyer (1985), 'The Costs of the Consensual Myth: Antitrust Enforcement and Institutional Barriers to Litigation in Japan', 94 *Yale Law Journal* 616–618.

70 See the report issued in May 1997 by the Intellectual Property Research Centre, p. 11-12. So far, in general, since the enactment of the Act only in six cases have plaintiffs invoked Article 25.

71 Although recently the FTC has been more positive in providing information for the civil courts, it is still insufficient for the litigants. See Akira Negishi (1996), *'Kōsei torihiki iinkai no kengen no kyōka' (The Str*engthening of the Power of the FTC), 1082 Jurisuto 147–148.

channels. In addition, the increase in US pressure and the Guidelines introduced in 1991 must be taken into consideration.

*Jeans case*

In one termination dispute the Osaka District Court denied the validity of a termination. For the first time a court considered the possible violation of the Anti-mo-nopoly Act an important factor for deciding whether 'unavoidable reasons' existed which could validate the cancellation. The dispute involved a manufacturer of high-quality brand-name jeans which had maintained a trade relationship with its distributor for 15 years. Problems started when the manufacturer demanded that the distributor stop reselling the jeans to another distributor through which the jeans reached a discount shop. After the distributor rejected the demand the manufacturer suspended supplies. It reasoned that the distributor had not regularly paid as was usual after the orders were delivered. In response, the distributor claimed that the termination amounted to a violation of Article 19 of the Anti-monopoly Act and was invalid. Subsequently, the distributor applied for three different injunctions. The first two claims were based on contractual rights. He sought legal confirmation that he had a contractual right to the supplies and he demanded the delivery of the goods which had been on order. The third claim was based on the general tort provision of Article 709 of the Civil Code in which he sought an injunction to ban the suspension of supplies in order to ensure future supplies.

The Osaka District Court granted the first two injunctions holding: "...in continuing supply contracts the seller can only stop supplies when there are unavoidable reasons. In this case the suspension of supplies was a measure to prevent the products from reaching a discounter and was done in order to restrict resale prices, which impeded fair competition. Therefore, the refusal to meet the demand of the producer does not constitute special circumstances such as a 'breakdown of the parties' trust relationship' which can justify this termination".

However, the court did not grant the third injunction since it contended that there was no legal basis for an injunction to supply the jeans in the future. The court held: "The refusal to deliver the goods to the distributor is an unfair trade practice and violates Article 19 of the Anti-monopoly Act. It is a serious violation of Nos. 2, 12 and 13 of the general designation. However, Article 20 of the same Act provides that the FTC can provide injunctions to stop the forbidden practice. In view of this Article it is clear that Article 19 of the Anti-monopoly Act does not directly provide a right for a demand of a private law injunction. In addition the distributor argues that a violation of this Article constitutes a tort which gives a right to an injunction to stop the refusal of supplies. However, tort suits are meant to demand compensation not to ask for injunctions. Therefore when there is only a right to damages there cannot be any such injunction".[72]

This decision has been often cited by legal scholars to confirm that private law injunctions based on a violation of the Anti-monopoly Act are not possible under Japanese law.

*Aloins Cosmetics case*

This case involved the question whether No. 12 of the general designation, prohibiting resale price maintenance, had been violated. In this case the Osaka District Court had favoured the potential infringement of the Anti-monopoly Act to justify its decision, whereas the Osaka High Court on appeal had only justified it on contract law. In this case the Osaka High Court did not reverse but rather slightly amended the District Court's decision. Ten years into the agreement a cosmetics manufacturer had cancelled the contract with a distributor which sold the products at below the indicated price. The distributor claimed the cancellation was invalid, among other things, because it had violated the Anti-monopoly Act and brought a suit for breach of contract and substitute damages. The District Court argued that the real reason for the termination was to maintain resale prices which violated the Act.[73] By contrast, the Osaka High Court held that the Act had not been violated and justified the invalidity of the cancellation primarily on contract law. There were no 'unavoidable reasons' for the termination of this distribution agreement.[74]

Particularly within the distribution system of luxury cosmetics a number of termination disputes involving anti-trust law issues have occurred. Within standard-form contracts concluded with their selected distributors, many manufacturers prohibit sales to other retailers such as discounters outside their own distribution system or impose certain sales methods upon the distributor which makes it difficult for them to sell at a discount or to resell to other retailers. Any violation of such impositions may then be a cause for termination based on a breach of contract. Most of the cases within cosmetics distribution centred around the question whether the imposition of such sales methods or the prohibition on reselling to other businesses can violate the Act. In some of these cases the District Courts have justified the invalidity of the termination partly on a violation of anti-trust law.

*Oppen Cosmetics case*

One case involved the validity of the requirement to sell door-to-door. In 1986 a distribution agreement was concluded between a cosmetics manufacturer and its distributor in which it was stipulated that the distributor would sell directly door-to-door. Four years into the agreement the distributor started to resell to discounters without adhering to the door-to-door sales clause. Subsequently, the manufacturer cancelled the agreement. The distributor responded by bringing a tort case claiming damages. He argued that he had not resold to

72 See the *Jeans case,* 1490 *Hanrei Jihō* 111 (Osaka District Court, 21 June 1993).

73 *Aloins Cosmetics case,* 1566 *Hanrei Jihō* 85, (Osaka District Court, 7 February 1995). Also in 1110 *Jurisuto* 165, with a note from A. Shōda.

74 *Aloins Cosmetics case,* 1612 *Hanrei Jihō* 62 (Osaka High Court, 28 March 1997). The amount of damages awarded by the District Court for projected profits for one year was reduced to projected profits for five months.

discounters and that the door-to-door sales clause was in violation of the Act (Nos. 2 and 13 of the general designation).

The Osaka District Court favoured the manufacturer which was upheld by the Osaka High Court on appeal. By attaching secret codes to some of its articles the manufacturer had found evidence of sales to discounters. On the alleged violation of the Anti-monopoly Act the court held: "the manufacturer's market share of cosmetics in Japan is only around 2 percent which is around 10th place in the country. Accordingly, these cosmetics have hardly any influence on the market. The distributor has always been able to obtain cosmetics from other manufacturers and it is not very difficult to shift trading partners. In view of these circumstances the door-to-door sales clause does not impede fair competition and does not violate the Act".

The distributor had also claimed that other contract provisions such as a pricefixing and a non-competition clause also violated the Act. He had invoked the informal warning *(keikoku)* earlier issued by the FTC against the manufacturer on 31 July 1991 in relation to the price-fixing clause it used in its contracts. However, the court held that the termination was not based on the violation of these clauses but rather on the violation of the door-to-door sales clause. Therefore the distributor's claim did not necessitate any further inquiry.[75]

### *Shiseido and Kao v.Discounters*

In some other recent famous termination disputes the validity of a face-to-face sales method was the central issue. In these disputes, which will be described in much more detail in the next chapter, twice the Tokyo District Court justified its decision to invalidate the cancellation of a distribution agreement partly on the potential infringement of anti-trust law.

However, both these decisions were reversed by the Tokyo High Court and have recently been confirmed by the Supreme Court. In these cases leading cosmetics manufacturers argued that their standard-form contracts required their distributors to carry out face-to-face sales, to attend seminars to learn how to conduct such sales and to keep a list of customers. They claimed that this sales method was necessary to maintain the quality of the cosmetics, to protect against potential skin irritation and as a result to benefit consumers. However, some distributors did not use this method and resold by mail order at a discount price. Manufacturers cancelled the agreement because of an alleged breach of contract.

In the first case the Tokyo District Court held that the obligation to carry out face-to-face sales is justifiable if such sales are necessary to ensure the safety of products, to protect the quality thereof, to maintain the goodwill of the products or to fulfil any other appropriate objectives. However, it had not been proved that the face-to-face sales method was designed to accomplish such goals. Rather, the court found that this sales method helped to discourage

75 *Oppen Cosmetics case,* 39 *Shinketsushū* 581 (Osaka District Court, 24 July 1992). Also described by T.Yamabe in 1065 *Jurisuto* 114; 40 *Shinketsushū* 667 (Osaka High Court, 14 September 1993).

distributors from discounting the price of the products and assisted in maintaining the manufacturer's suggested resale price. Accordingly, the Court concluded that: "the obligation to carry out the face-to-face sales violated the 'spirit' of the Antimonopoly Act. Therefore, the termination of the contract by the manufacturer was not justifiable and was therefore null and void".[76] These statements by the court were very similar to the section on the restriction of sales methods in the Guidelines of 1991.[77]

In a second similar case the Tokyo District Court went even further and held that the cancellation was an abuse of rights and the provisions in the contract requiring face-to-face sales were considered to be a 'serious' violation of the Anti-monopoly Act.[78]

On appeal, both decisions were overturned by the Tokyo High Court which based its decisions primarily on contract law. In relation to a possible violation of the Anti-monopoly Act the Tokyo High Court argued in the first case that the face-to-face sales requirement may lead to price stability but such effect in itself does not lead to a violation of the Act. For a violation circumstances must be found which establish that this sales method functions as a means to restrict resale prices. The court held that there had not been sufficient evidence to prove such causal relationship.

Furthermore, the Court held that the requirement of face-to-face sales is reasonable, given the nature of luxury cosmetics, and found that such requirements are not prohibited when they are necessary or helpful in ensuring proper sales of the product, product safety, quality control and maintenance of goodwill and if they are imposed in a similar way on all other trading partners. In this way it implicitly referred to what the Guidelines state in relation to No. 13 of the general designation on the restrictions on sales methods. Finally, the court held that businesses are free to decide which sales policy or sales method they wish to adopt.[79] In the second case the Tokyo High Court also found for the manufacturer and put for ward similar arguments about the possible violation of the Anti-monopoly Act. However, on this occasion the court explicitly referred to what the Guidelines state on No. 13 of the general designation. Furthermore, in this case it found it to be of importance that the share of the manufacturer's products was only 3.7 percent of the total market, which means that market control was not so extensive.[80]

The two Tokyo High Court decisions have recently been confirmed by the Supreme Court which based its decision entirely on anti-trust law and has provided for the first time a general rule on a violation of No. 13 of the general designation. The Supreme Court held:

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76 *Shiseido v.Fujikihonten,* 1474 *Hanrei Jihō* 25 (Tokyo District Court, 27 September 1993).

77 The court made the mistake, however, of calling the practice of Shiseido an unreasonable restraint of trade, which only applies to cartels where it should have called it an 'unfair trade practice'. See K.Kawagoe (1993), *'Hanbai hōhō ni kansuru yakujō to tokuyakuten keiyaku no kaiyaku'* (Termination of Distribution Agreements and the Clauses Related to the Sales Method), 533 *New Business Law* 15.

78 *Kao v. Egawakikaku,* 1500 *Hanrei Jihō* 3 (Tokyo District Court, 18 July 1994).

79 *Shiseido v. Fujikihonten,* 1507 *Hanrei Jihō* 43 (Tokyo High Court, 14 September 1994).

> … There are various kinds of dealings on restrictive terms and therefore the likelihood of an impediment to fair competition depends on the nature and the degree of the restriction. Only in case it is likely to exert a detrimental influence on the fair competition order, does that correspond to dealings on terms which 'unjustly' restrict the activities of the other party. In view of the fact that the freedom of choice as regards the sales policy and the sales method of a manufacturer or wholesaler must be respected, we conclude that as long as the restrictions on the sales method imposed upon the retailers (for example, giving directions about the method of product display and product maintenance and obliging them to give explanations to the customers) are based on reasonable grounds for the sale of such products and as long as similar restrictions are imposed upon the other trading partners, they do not exert a detrimental influence on the fair competition order and therefore do not correspond to dealing on terms which 'unjustly' restrict the business activities of the other party as stipulated in No. 13 of the general designation.

Applied to this case the Supreme Court found that the obligation to sell face-to-face is reasonable since it functions to maintain the brand image of these products. Furthermore, the manufacturers have concluded similar contract clauses with other trading partners and therefore it does not correspond to dealing on terms which 'unjustly' restrict the business activities of the other party.

In both cases the Supreme Court used similar arguments but in the second case the Court also dealt with the question whether the prohibition on reselling to other retailers violated the Anti-monopoly Act. The Court found that: "If cosmetics are being resold to retailers which have not concluded distribution agreements and which are not obliged to sell face-to-face, the purpose of the distribution agreement to maintain the brand image of the Kao cosmetics, can no longer be realised. Therefore, the prohibition on sales to retailers with which Kao has not concluded this agreement must inevitably go together with a duty to sell face-to-face. In case the face-to-face sales clause is not held to violate Article 19 of this Act, automatically such a prohibition does therefore also not contravene this Article".[81]

For the first time the Supreme Court had issued a general rule on this issue and to some extent it may have gone against the relevant articles in the Guidelines as regards No. 13 of the general designation.[82] It is important to note, however, that the Supreme Court has not provided any clarification about the exceptional circumstances under which the face-to-face sales system may indeed violate the Anti-monopoly Act.[83]

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80 *Kao v. Egawakikaku,* 1624 *Hanrei Jihō* 55 (Tokyo High Court, 31 July 1997).

81 *Shiseido v. Fujikihonten,* 1664 *Hanrei Jihō* 3 (Supreme Court, 18 December 1998). *Kao v. Egawakikaku,* 1664 *Hanrei Jihō* 14, (Supreme Court, 18 December 1998). These decisions can be viewed as somewhat similar to the approach on selective distribution agreements by the EU Commission and the Community Courts.

## 4.5 Japanese Legal Literature

The increasing number of cases in which distributors invoke anti-trust law before the civil courts and the resulting appearance of some District Court decisions, which are justified on the violation of the Anti-monopoly Act, is concurrent with recent developments in Japanese legal doctrine.

At first, legal scholars in Japan did not recognise or study the inseparable relationship between civil law and anti-trust law. For civil law scholars anti-trust law was merely a product of foreign pressure and they focused on the points of friction between the two laws. Experts in anti-trust law similarly emphasised these frictions, arguing that anti-trust law had appeared to correct the civil law principle of freedom of contract which supports free competition without interference. Furthermore, they stressed that the Civil Code is a law regulating the rights and duties between individuals. Disputes only reach the courts upon the initiative of these individuals. In contrast, the Anti-monopoly Act is a law for the public good supporting fair and free competition. This law is more actively enforced mainly by an administrative agency, the FTC.[84]

Therefore, when interest grew in this topic initially many legal scholars did not support a general invalidity of acts which violated the Anti-monopoly Act. This may also have been caused by a lack of experience with the Act and the notion that trade among individuals should not be influenced by economic policies. Another reason may be that in Japanese society the policies to protect competition did not have much legitimacy. Until recently the notion that it is worthwhile to protect competition had not been strong. Since the middle of the 19th century the value of competition had been looked down upon.[85]

Recently, there has been a sharp increase in academic writings about this issue[86] and most legal scholars support a more constructive role of civil law in order to protect competition.[87] This is concurrent with the recent increase in the legitimacy of anti-trust law in Japan. This has not only been caused by US pressure but by the growing notion among people that it is worthwhile to protect competition and to secure a free market.[88] Among many legal scholars more interest has grown in incorporating competition into the 'public order' principle of private law. Currently many legal scholars argue that a violation of the Act may constitute a violation of Article 90 of the Civil Code.

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82 This will be explained in the next chapter.

83 According to legal scholar Masahiro Murakami this has been a wise decision of the Court because such clarification should be entrusted to the development of future theory and practice. See Masahiro Murakami (1999), *'Shiseido Kao jiken saikōsai hanketsu no nokoshita kadai'* (Remaining Issues after the Supreme Court Decisions in the Shiseido and Kao Cases), 667 *New Business Law* 12.

84 See Akira Negishi (1994), *'Minpō to dokusen kinshihō'* (Civil Law and the Anti-monopoly Act), 46 *Hōsō Jihō* Nos. 1, 2 p. 1–2.

85 See Atsushi Ōmura (1993), *'Torihiki to kōjo, hōrei ihankōi kōryokuron no saikentō'* (Trade and Public Order, a Re-examination of the Theory of the Validity of Acts Violating Statutes), 1025 *Jurisuto* 67.

However, according to one influential school this depends on the nature and the degree of the violation. Furthermore, whether or not an illegal act or contract is unenforceable depends on the circumstances under which such act or contract is made. This school holds that once the act or contract has been performed, it should be treated as valid. This theory, called the 'theory of restrictive nullity' *(seigen mukō setsu)* tries to harmonise the need for the protection of innocent third persons and the necessity for strong enforcement of the Act. For example, legal scholar Masahiro Murakami supports this theory arguing that the judgement on whether an act falls under Article 90 of the Civil Code and is therefore null and void, should be made on a case-by-case basis. It depends on such factors as the purpose of the forbidden provisions, the degree of illegality of the act and the legal security of transactions.[89] It is important to realise that the private law effect may differ according to the type of violation. For example, price fixing contracts are in principle null and void, but this does not always apply to acts constituting unfair business practices such as dealings on unjust restrictive terms.[90]

Another school which has recently gained more ground, supports the general invalidity of acts in violation of the anti-trust law.[91] The notion has gained strength that when there is a violation of the Anti-monopoly Act it automatically renders the action null and void. Legal scholars who support this rule point to some of the recent cases in which the lower courts have held certain acts to be void because of a violation of the Act.[92]

Finally, it is interesting to note that some legal scholars have pointed to some recent court decisions and suggest that a useful incorporation of anti-trust law into civil law is to consider a violation of the anti-trust law as one factor of importance in whether 'unavoidable reasons' exist for the cancellation.[93] Because there are many different ways in which anti-trust law may be violated, this approach may provide the courts with more flexibility.[94]

The Japanese legal scholar Tadashi Shiraishi has described the relationship between anti-trust law and contract law from a different angle. According to him the requirement in

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86 For a broad analysis of legal doctrine, see, Hirō Sono (1996), *'Dokkinhō ihan kōi no shihōjō no kōryokuron'* (Discussion on the Private Law Effect of a Violation of the Anti-monopoly Act), *Kanazawa Hōgaku* Volume 38, No. 1–2, p. 263–297.

87 A.Ōmura (1993), o. c., 1023 *Jurisuto* 82–89 and 1025 *Jurisuto* 66–74; See Akira Negishi (1994), o. c., p. 1; See also Minjiteki Kyūsai Seido Kenkyūkai (The Research Committee on the Civil Remedy System) and Mitsuo Matushita (eds.) (1997), *Fukōsei na kyōsō kōi to minjiteki kyūsai* (Civil Remedy and Unfair Competition Acts), *New Business Law (Bekkan)* (Separate Volume) (1997) No. 43, p. 88.

88 See A.Negishi (1994) o. c., p. 2–3.; and A.Ōmura (1993), o. c., p. 68.

89 See Masahiro Murakami (1999), *'Shiseido Kao jiken saikōsai hanketsu no nokoshita kadai'* (Remaining Issues after the Supreme Court Decisions in the Shiseido and Kao Cases), 667 *New Business Law* 14.

90 See C.Heath (1995), o. c., p. 102–103.

91 Noboru Kawabe (1996), *'Dokusen kinshihō to shihō torihiki'* (Civil Trade and the Anti-monopoly Act), 1095 *Jurisuto* 170; Mitsuo Matsushita (1986), *'Dokusen kinshihō ihan o meguru minji soshō ni kansuru hanrei bunseki'* (Analysis of case law in relation to civil suits concerning violations of the Anti-monopoly Act), 535 *New Business Law* 6, 534 *New Business Law* 27; See also the report, issued in May 1997 by the Intellectual Property Research Centre, p. 37.

contract law of 'unavoidable reasons' for a valid termination of a continuing contract is close to the notion of 'abuse of a dominant bargaining position' which is prohibited under No. 14 of the general designation. They may even complement each other.[95] Although doubts may be raised about whether a cancellation may correspond to an abuse of a dominant bargaining position the latter notion may satisfy the lack of regulation concerning the termination of trade relationships because of non-compliance with disadvantageous trade conditions.[96]

### *Recent Moves towards Stronger Private Law Enforcement*

Finally, it is important to point to the recent initiatives in Japan to propose a stronger private enforcement of anti-trust law in general. Accordingly, this might also have an effect on the possibilities for distributors to invoke anti-trust law after unilateral terminations of distribution agreements.

Many legal scholars contend that there should be more reliance upon the people to enforce the Anti-monopoly Act. These initiatives were started under the control of the Ministry of International Trade and Industry (MITI). The main proposal is the introduction of private law injunctions before the civil court if the Act is violated. In addition, proposals have been made for better access to the civil courts and a simpler use of Article 25 of the Act and Article 709 of the Civil Code.[97] These initiatives have had an effect since the Japanese Government has drawn up a proposal to help create a civil litigation system enabling victims of unfair trade practices to more easily take their cases to court.[98]

The FTC itself is also undertaking research on this topic and has obviously competed to some extent with the MITI. It has also requested many law professors which are experts on this field to participate in this research and to issue reports. Recently on 22 October 1999 a report was published by a research committee under the control of the FTC.[99] It proposes both the introduction of private law injunctions before the civil court if the Act is violated and a simpler use of Article 25 of the Act and Article 709 of the Civil Code.

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92 T.Shiraishi (1997), o. c., p. 150.

93 T.Shiraishi (1998), *'Keiyakuhō no kyōsō seisakuteki na ichi danmen'* (One Aspect of Contract Law in its Policy on Competition), 1126 *Jurisuto* 132.; and H.Nakata (1994), o. c., p. 495–496.

94 H.Nakata, (1994) o. c.,p. 496.

95 T.Shiraishi (1998), o. c., p. 125–132.

96 Ibid.,p. 126.

97 In some reports many suggestions have been made for a stronger private law enforcement of the Act. See for example the report issued in May 1997 by the Chiteki Zaisan Kenkyūsho (Intellectual Property Research Centre) also in: *New Business Law (Bekkan)* (Separate Volume) No. 44 (1997); The report of the Minjiteki Kyūsai Seido Kenkyūkai (The Research Committee on the Civil Remedy System) also headed by Mitsuo Matsushita and published in: *New Business Law (Bekkan)* (Separate Volume) No. 43 (1997); and a report by the Kigyō Hōsei Kenkyūkai (The Research Committee on Business Law Systems) referred to by Kazuhiko Bandō in: 644 *New Business Law* 11–17 (1998).

After consultations with the Ministry of Justice the FTC planned to reach a conclusion by March 2000 and to introduce a bill in the Diet.[100]

Some reports also refer to the possibility of a private law injunction for discounters after their supplies have been cancelled by manufacturers in order to maintain resale prices. However, although some members support the introduction of a claim to supply the distributor, the reports concluded that such an injunction is very difficult.[101] In principle injunctions take the form of ordering a company to refrain from carrying out a certain action, not of ordering it to actively perform an act. Therefore, a possible injunction can only be a prohibition to refuse supplies which will probably lack effectiveness. This is because manufacturers may be able to argue that they have cancelled for other reasons. Furthermore, in view of the principle of freedom of contract manufacturers are free to trade with whom they want and an injunction to actively supply another company may be going too far. Securing the effectiveness of such an order becomes a problem for civil executory law.[102]

Therefore, a suit for specific performance based on a contractual right probably remains the best option for a distributor even if such a new injunction procedure is introduced. One legal scholar contends that such an injunction might only be useful when the civil court has not accepted such a contractual right for performance.[103]

## 4.6 A Brief Comparison with EU and Dutch Anti-trust Law

Also in the Netherlands increasing importance is being attached to the private law enforcement of EU and Dutch anti-trust law. There are comparable problems in the Netherlands for such private law enforcement as in Japan and case law is not very different. One major difference, though, is that the Commission and the Dutch National Competition Authority more strongly support an active role of the civil courts in enforcing anti-trust

98 The purpose is to prevent a possible surge in business disputes arising from the deregulatory measures currently being introduced. See also *Nikkei Weekly* June 8, 1998.

99 The report issued on 22 October 1999 by the Research Committee on the Civil Remedy System in Relation to Violations of the Antimonopoly Act *(Dokusen kinshi ihan kōi ni kakaru minjiteki kyūsai seido ni kansuru kenkyūkai)*. Partly explained by Masanori Tsukada (1999), in: 678 *New Business Law* 18–26.

100 *Nihon Keizai Shinbun,* 23 October 1999.

101 Kazuhiko Bandō (1998), *'Fukōsei na kyōsō kōi ni taisuru minjiteki kyūsai seido ni kansuru shuyō ronten —Kigyō hōsei kenkyūkai hōkokusho o sozai ni shite'* (Main Issues in relation to the Civil Remedy System in respect to Unfair Competition Acts—Based on the Report of the Research Committee on Business Law Systems), 644 *New Business Law* 14–15.

102 The report of the Research Committee on the Civil Remedy System headed by Mitsuo Matsushita published in: 43 *New Business Law (Bekkan)* (Separate Volume) (1997) p. 22–23.

103 See Yoshiyuki Tamura (1996), *'Kyōsōhō ni okeru minji kisei to gyōsei kisei'* (Civil Regulations and Administrative Regulations in Anti-trust Law), 1088 *Juristo* 65–66.

law. This is also evidenced by Article 81(2) of the EU Treaty and its Dutch equivalent, Article 6 of the new Dutch Competition Act which automatically renders a contract (clause) in violation thereof null and void.

However, Dutch distributors face comparable difficulties as distributors in Japan. As in Japan, suppliers will usually not justify the termination of a distribution agreement on a non-compliance of a forbidden trade practice. Furthermore, so far the enforcement of EU and Dutch anti-trust law before Dutch civil courts is also still relatively underdeveloped. Courts are hesitant to apply anti-trust law in part because of similar reasons as in Japan. This consists of a lack of familiarity of judges with anti-trust issues and difficulties in finding sufficient proof of a violation for the plaintiff. Anti-trust law is also not a compulsory subject in Dutch law faculties.

Nevertheless, generally speaking, many factors such as the procedural barriers and less clarity in anti-trust law in Japan caused by weaker and more informal public law enforcement, may make it more difficult for Japanese distributors to invoke the Act before the civil courts. Furthermore, it is important to realise that in Japan a contract, which is in violation of the Anti-monopoly Act, is not automatically null and void.

## 5
## COMPLAINT WITH THE FTC

### 5.1
### Complaint

Instead of, or in addition to, commencing a civil suit, distributors may file, or threaten to file, a complaint with the FTC, requesting it to take measures, when they believe that the termination of the distribution agreement or the refusal to trade has violated the Anti-monopoly Act.

Article 45 of the Anti-monopoly Act stipulates that any person can request the FTC to institute an investigation as regards any suspected violation of the Act and can ask for necessary measures to be taken. Although exact figures are not available[104] it is highly probable that on many occasions distributors have demanded that the FTC should take measures after manufacturers have suspended or limited supplies.[105] In some cases distributors have commenced civil litigation only after their complaint with the FTC had been rejected.[106]

Whether or not an investigation is conducted is left to the discretion of the FTC. Article 45(3) stipulates that if the complaint includes some concrete facts in writing the FTC will notify the complainant of the type of measure it has or has not taken in the case.[107] However, when the FTC decides not to take measures it rarely explains the reasons therefor.[108] Furthermore, the complainant does not have any further means to challenge such a decision.

104 When I visited the FTC on 25 November 1997, I was told that such information was not available.

The complainant does not have any inherent right to any measures.[109] It must be noted that the General Secretariat consists of just over 500 people and can only investigate a small amount of all claims. It has usually set its priorities and accordingly the cases investigated can largely be predicted.[110] On average the FTC investigates around 200 cases a year. One additional problem is that in addition to their headquarters in Tokyo there are only eight local offices of the General Secretariat in the country which can make it more difficult for distributors in outlying areas to file a complaint.[111]

Even if the FTC decides to take measures against the violator after it has found in its investigation that the Act has been violated, this still cannot always directly help the distributor. The FTC can order the violator to cease a forbidden trade practice such as resale price maintenance and take appropriate measures, but it cannot demand that the violator actively resumes supplies to the distributor.[112] However, the threat of a sanction by the FTC may cause the violator to resume supplies on its own initiative.

### 5.2
### Indirect Influence upon the Civil Courts

When a complaint turns out to be successful it may have an indirect influence upon civil proceedings. This is because the findings of the FTC can be brought forward before the

105 In general, there are many cases in which companies have complained but the FTC has not taken any action. Therefore, it can be assumed that distributors also frequently file complaints. See Takuya Sekiguchi (1997), *'Dokusen kinshihō ihan kōi ni taisuru minjiteki kyūsai seido no kentō'* (A Study of the Civil Remedy System in relation to Violations of the Anti-monopoly Act), 625 *New Business Law* 19.

106 *Shiseido v. Fujikihonten,* 1507 *Hanrei Jihō* 43 (Tokyo High Court, 14 September 1994) and *Shiseido v. Kawachiya 41 Shinket*sushū 501 (Urawa District Court, 17 February 1995). Also in M.Murakami (1995), *'Keshōhin ryūtsū o meguru dokusen kinshihō ihan jiken no bunseki'* (Analysis of Violations of the Anti-monopoly Act in relation to Cosmetics Distribution), 579 *New Business Law* 28–31.

107 Article 19(1) of the internal rules of the FTC *(shinsa shinpan kisoku)* provide that these concrete facts must include the name and address of the complainant, the names of the companies in violation of the Act and the exact facts (time and place) of the violation.

108 T.Shiraishi (1997), o. c., p. 140. One reason for the FTC not to take any measures may be that the act in question does not widely occur.

109 *Ebisu shokuhin kigyō kumiai case, Minshū* 26, No. 9, p. 1573 (Supreme Court, 16 November 1972).

110 Kenji Kawagoe (1997), in: *Nikkei Business,* 3 November 1997.

111 The FTC planned to open clinics at 3,300 local Chambers of Commerce for those who have suffered from unfair business practices. In this way many small companies in areas other than the headquarters and the eight offices have more possibilities to report unfair trade practices. See *Nikkei Weekly,* 24 August 1998.

112 Y.Tamura (1996), o. c, p. 65–66. Even if such an injunction would be granted the manufacturer may refuse to accept it, which may lead to a long-lasting hearing procedure. Such procedures are not helpful for the distributor who needs an expeditious interim measure.

civil courts. Furthermore, distributors can make use of earlier similar complaints by other distributors against the same manufacturer when they have turned out to be successful.

However, it must be noted that the interrelation between the decisions of the FTC and the decisions of the civil courts is not very clear. Formally, the civil courts are independent of the FTC and are not bound by its decisions.[113] They can only be used as a reference, which means that the civil courts may come to different conclusions than the FTC. The Japanese Constitution proclaims that the final interpretation of laws is in the hands of the courts. Furthermore, Article 85 of the Antimonopoly Act provides that FTC decisions can be reviewed by the Tokyo High Court.

Nevertheless, the Japanese legal scholars are divided on this issue. One school argues that FTC decisions are always binding upon the courts, while a second school holds that these decisions only have a 'presumption value' *(suitei ryoku)* and the courts may deliver a different decision than the FTC. Finally, a third school takes an intermediate position. It only acknowledges the binding force of 'hearing' decisions, whereas recommendation decisions or consent decisions only have a presumption value.[114]

Another problem is that in the event that the FTC takes measures, these are usually informal, such as warnings or cautions, which do not formally establish that the Act has been violated. Even more formal measures such as recommendation decisions or consent decisions may not necessarily help the distributor very much in gathering sufficient evidence. These decisions are not based on a finding of a violation based on evidence but are based solely on the respondent's agreement to accept the decision voluntarily.[115] Only a hearing decision after the completion of a hearing procedure might provide sufficient proof for a violation because such decisions are based on a finding of a violation proved by evidence.[116]

## 6 CONCLUSION

In summary it can be concluded that it is difficult for distributors in termination disputes to successfully invoke the Anti-monopoly Act. So far, distributors have had little success in invoking the Act before the civil courts. There are still many barriers for the distributors.

First, there is not sufficient clarity for distributors about the exact relationship between the Anti-monopoly Act and the Civil Code. These Codes do not contain any provisions which may provide clarity about this relationship. Furthermore, Japanese case law is divided about the private law influence of acts in violation of the Anti-monopoly Act.

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113 863 *Hanrei Jihō* 20 (Supreme Court, 19 September 1977).

114 Kenji Kawagoe (1997), *Dokusen kinshihō* (The Anti-monopoly Act), p. 430–431.

115 M.Murakami (1997) o. c., p. 81; H.Iyori (1997), o. c., p. 615. K.Kawagoe argues that within the recommendation and consent decisions, there is a column with facts *(jijitsu),* which should not be ignored by the courts. See K.Kawagoe (1997), Ibid., p. 431.

116 It must be noted that such a hearing decision may not be final in case the respondent decides to commence proceedings to quash the FTC decision before the Tokyo High Court.

Second, the relationship between civil procedural law and the Anti-monopoly Act is also vague and rather problematic. This also concerns the complicated relationship between the FTC and the civil courts. For example, collecting evidence proves very difficult for distributors. This not only applies to private suits for specific performance or damages based on the Civil Code but also to the private suit for damages as regulated by the Anti-monopoly Act itself (Article 25).

Finally, there is still insufficient information for distributors as to what kind of termination, or clauses justifying it, may constitute a violation. This is mainly caused by the more informal enforcement of the FTC and the corresponding limited number of legal precedents in the form of formal decisions by the FTC and the Courts. Accordingly, there has been much reliance upon the Guidelines of 1991. They, however, still leave many questions open and have hardly been challenged by formal FTC or Court decisions. Generally speaking, there is much insecurity concerning the exact legal position of the Guidelines. They are presented as 'informal' but have a great deal of impact in actual legal practice. In Japanese legal practice no clear distinction is made between the Guidelines and formal law as embodied in the Codes and case law.

In my opinion, the lack of clarity about the relationship between the Anti-monopoly Act and the other laws and the lack of clarity about which kind of acts may constitute a violation of the Act is aimed at preserving a great deal of discretionary power for the FTC. It seems that the FTC does not want to lose its power by becoming bound to a great number of legal precedents. Private suits in which the Act is invoked are not stimulated. Furthermore, in contrast to the public law enforcement of the Anti-monopoly Act by the FTC, the private law enforcement of the Act is unpredictable since parties can bring forward various issues at any time.

Therefore, an increase in the number of decisions by the civil courts is very important for the creative development of law and for distributors who want to invoke the Anti-monopoly Act in termination disputes. Recently, distributors have increasingly made use of the private law enforcement of anti-trust law after terminations of distribution agreements, which for the first time has led to some important and influential court decisions.

First, some District Courts have started to use anti-trust law in order to justify their decisions. Although they have almost all been overturned on appeal by High Courts this may still illustrate the important 'progressive' role of District Courts in Japan.

Second, civil courts can provide more clear rules on the actions which may constitute a violation of the Act. For example, although the recent Supreme Court decision has made clear that the face-to-face sales method used in the luxury cosmetics industry does not violate the Act, it has still given some clarification and has maybe even contravened the Guidelines to some extent.

Finally, although the number of such court decisions in which anti-trust law was applied is still limited, the growing legitimacy and the stronger enforcement of the Act may have given distributors more means by which to fight large manufacturers in court. Civil litigation

can be accompanied by a complaint before the FTC. Furthermore, the initiatives for a stronger private law enforcement of the Anti-monopoly Act may also benefit distributors.

A brief comparison with EU and Dutch competition law shows that there are many similarities in the difficulties experienced by distributors in invoking anti-trust law in termination disputes. Nevertheless, as will be described in chapter 5, Dutch distributors have somewhat more possibilities than their Japanese counter-parts. There is more clarity as to what kind of actions are in violation of EU and Dutch anti-trust law. Furthermore, the relationship between both EU and Dutch anti-trust law, on the one hand, and other laws, on the other, is more clearly defined.

# 4
# Termination Disputes within the Japanese Distribution System for Luxury Cosmetics A Case Study: Manufacturers v. Discounters

## 1
## INTRODUCTION

Japanese manufacturers of luxury cosmetics sometimes terminate distribution agreements with their distributors. In most cases it concerns distributors, which were no longer able to pay the purchasing price.[1] Terminations of distribution agreements have rarely generated any legal termination disputes.

However, at the beginning of the 1990s major termination disputes started when leading manufacturers of luxury cosmetics such as Shiseido, Kao, Kanebō, Kosé and Max Factor terminated distribution agreements with some of their distributors who were selling at a discount. Several discounters resisted and filed complaints with the FTC against these manufacturers. They claimed that the termination of the contract amounted to an infringement of the Anti-monopoly Act.

In addition to filing complaints with the FTC some discounters also brought a suit before the civil courts. They demanded a declaration that they still had a right to receive the supplies based on the contract and demanded the supply of the cosmetics which had been on order. These legal disputes generated a great deal of publicity in Japan and led to a number of court decisions in which both contract law and anti-trust law were influential. They reflect the power struggle between leading cosmetics manufacturers and several of their distributors who did not abide by their marketing policies.

These disputes must be viewed against the background of significant pressures to lower prices caused by a period of stagnant economic growth in the Japanese economy which began in the 1990s. The decrease in the Japanese consumers' purchasing power triggered the sudden growth of discounters which had many repercussions in the distribution sector. Furthermore, it is important to take into consideration the mounting US pressure starting with the 1989 Structural Impediments Initiative talks between Japan and the US, which led to the promulgation of the Guidelines in 1991 concerning the distribution system and business practices.[2]

A detailed case study of these termination disputes may offer many insights, which have largely become lost in general assumptions about the role of law in Japan. First, these case studies may provide some illustration of the influence of contracts and contract law when

distribution agreements are terminated by manufacturers. They may give insights into contract practice and contract consciousness within the luxury cosmetics industry in Japan. Second, they serve to illustrate the influence of anti-trust law which plays a very important role within these termination disputes. Third, they demonstrate the subtle interplay between contract law and anti-trust law, the Japanese civil courts and the FTC. The focus in these case studies is directed towards the possibilities in actual practice for distributors to take legal action if distribution agreements are terminated by their manufacturers/suppliers.

In this chapter these disputes are described in some detail. I have followed discounters of luxury cosmetics who have initiated legal procedures in the 1990s in the region of Tokyo after their contracts were terminated. These distributors/discounters were usually larger than the regular distributors and were therefore able to take on such large manufacturers. [3] In a descriptive and chronological way the developments of these disputes are described, after which some conclusions will be drawn. However, first, a short overview of the cosmetics industry and its distribution system is given with its development over time. I will describe the relationship between leading manufacturers and selected distributors in order to become familiar with the business and legal relationships that existed between leading manufacturers and distributors before the termination disputes.

During my stay as a researcher at the University of Tokyo from April 1993 to March 1995 I started collecting material about these disputes. The facts of the case studies are based on primary and secondary material. Secondary material consists of articles in Japanese newspapers, legal and economic journals. Furthermore, general information about the cosmetics distribution system has been obtained through official reports from government agencies and books about this industry.

The primary material investigated consists of standard-form contracts used by the large manufacturers of luxury cosmetics and legal documents associated with the lawsuit such as copies of official court decisions and briefs. In addition, I gathered much information by means of 14 interviews, which were conducted in the Japanese language with many people directly or indirectly involved in these termination disputes.

### *Interview Approach*

These interviews were made possible by my supervisors Professor Yoshihisa Nōmi and Professor Takashi Uchida of the Law Faculty of the University of Tokyo who asked Mitsuo Matsuzawa, the General Editor of the Commercial Law Centre *(shōji hōmu kenkyūkai),* to arrange these interviews. The Commercial Law Centre publishes many books and journals

1 For example, Takafumi Uchida of the legal department of Shiseido, Personal communication, 20 November 1997; and Mr Nakanō from the sales department of Kao, responsible for legal matters,

2 Personal communication, 14 November 1997. See, A.Yamada, M.Ōkuma and N.Narasaki (1991), *Ryūtsū torihiki kankō ni kansuru dokusen kin shihō gaidorain* (The Anti-monopoly Act Guidelines concerning Distribution Systems and Business Practices).

and has a great deal of connections with Japanese businesses, government bureaucracy and universities.[4] Through the connections of Mitsuo Matsuzawa these interviews could be arranged. I wanted to hear the story from both sides in order to remain objective and therefore I asked for interviews with the representatives of the two most important manufacturers of luxury cosmetics which were involved in the disputes and the President (and his lawyer) of the most important discounter under whose leadership some other discounters also started to take on the manufacturers.

I also asked for an interview with a civil court judge who had rendered a decision on these cases and an official of the FTC. Furthermore, I requested interviews with third party observers such as a journalist, an editor of a magazine on the cosmetics industry and a bureaucrat from MITI who had much information about this industry. All these requests were honoured and the judge I asked for turned out to be the presiding judge of the Tokyo High Court who had rendered a very influential decision in these cases. This means that there were no negative responses. Finally, Mitsuo Matsuzawa also came up with his own suggestions and arranged an interview with a former Commissioner of the FTC.

I conducted these interviews during two different periods. Sometimes the same people were interviewed during both these periods. The first interview sessions were held during the second half of 1994. In this period all of these legal disputes were running and had already led to some court decisions which had generated much publicity. The second interview sessions were held during the month of November 1997. At this stage most decisions of any importance had already been rendered by the civil courts and the FTC and there was much less publicity than previously.

I conducted open semi-structured interviews in which my approach was as follows: First, when I interviewed the people directly involved in these disputes, I focused on the facts without enquiring about their opinions. Based on a chronological list of facts, as I understood them from court decisions and articles in Japanese newspapers, I asked them to give me their version of the facts and to explain the motives for their actions. I was very interested in the time-span between subsequent events in these disputes and when a particular event had taken a long time, I asked them about the reasons therefor. Accordingly, these interviews served to discover more about the motives for the actions of the people involved and to complete the data.

When I interviewed the third-party observers I not only asked them for their version of the facts as neutral observers, based on a similar list, but also inquired about their opinions on these termination disputes. Finally, when I interviewed the Tokyo High Court judge I asked him, among other things, about his experience with these kinds of disputes and how he had reached his decision. During most of these interviews I also asked for important

3 Apart from some cases in the Osaka region which are described in the previous chapter, it is likely that these were the only termination disputes between manufacturers of luxury cosmetics and discounters. During my interviews with manufacturers and discounters they could not inform me of any other termination disputes with discounters including disputes which did not lead to a court decision and which did not generate any publicity.

legal documents such as contracts and other material. Furthermore, I asked for some general background information about the luxury cosmetics industry.

First, on 23 May 1994 I conducted an interview with two employees of the head company of Shiseido, Takafumi Uchida, manager of the Corporate Relations Department, and Hiroshi Kubo of the General Office Administration Department in the legal affairs section. Both Shiseido employees were accompanied by Shiseido's outside lawyer from the Ishii Law Office, Shūhei Sakurai. Thereafter on June 12,1 interviewed Motoshi Fujii, the Executive Director of the Japan Cosmetic Industry Association. In December 1994 several interviews were conducted shortly after one another: On 7 December with Hidehito Takizawa, a staff writer of the marketing news department of the Editorial Bureau of the Nihon Keizai Shinbun *(Nikkei),* who had closely followed these cases; on 13 December with Jirō Yamane, the lawyer representing some of the discounters; on 14 December with Tetsuya Hamabe, the Deputy Director of the Bio-chemical Industry Division of the Basic Industries Bureau of MITI, which gathers much information about the cosmetics industry; and finally on 26 December with the Presiding Judge of the Tokyo High Court, Kin'ichi Takahashi and one assistant judge Sadao Oyokawa who had passed judgement on the most influential termination dispute between Shiseido and one of its distributors Fujiki.

During the month of November 1997 I conducted the following interviews: on 7 November with Ikuo Yamamoto of the editorial staff of *Kokusai Shōgyō,* a monthly magazine for the cosmetic, toiletry and drug industries; on 10 November for the second time with Jirō Yamane, this time at his office in Matsumoto city; on 13 November with Ken Fujisawa, president of one of the discounters, Fujiki; on 14 November with three employees of Kao, Mr Nakanō of the Sales planning group of the General Sales Section, Yasuyuki Sasayama, Assistant Manager of the Legal Department and Toshiaki Hideshima, Manager of the Legal Department; on 19 November for the second time with Hidehito Takizawa and subsequently on the same day with Hiroshi Iyori, a former Commissioner of the FTC and a Professor of law at Chūō University; on 20 November for the second time with Shiseido, which this time attended with five employees of the newly formed legal department of the Shiseido head company. Two of them I had earlier interviewed in 1994, Takafumi Uchida and Hiroshi Kubo; and finally on 25 November with Mr Ishitani, sub-section head of the Trade Practices Bureau of the FTC.

For these interviews only Kao and the FTC had asked me to send my questions in advance. Mr Matsuzawa was present during all the interview sessions. Professor Takashi Uchida was present during the interviews with Kao, Shiseido, the Tokyo High Court judge and the journalist of the Nihon Keizai Shinbun. These interviews were held in the Japanese language and were recorded on tape with the approval of the respondents. I followed the advice not to mention during my interviews with the large cosmetics manufacturers the fact that I had already conducted interviews with the president of Fujiki and his lawyer, Jirō Yamane.

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4 The Commercial Law Centre is located in the Tokyo Tatemono Higashiyaesu Building. 2–27–10, Hatchōbori, Chūō Ward, Tokyo.

At the end of November 1998 I sent the quotations of Kao, Shiseido, the Tokyo High Court judge and both the president of Fujiki and his lawyer for approval to Japan. Based on the Japanese tapes I have used some important passages, which I have translated into English for this chapter. I wrote letters to the respondents in Japanese in which I asked for their approval of the quotations. I literally attached the English text and a retranslation into Japanese. The letters were first sent to Mitsuo Matsuzawa whom I asked to send them on to the respondents with a personal note. On March 1999 I received a letter from Matsuzawa in which he had written that Kao completely approved of my quotations. However, he wrote that Shiseido had modified a few of my quotations and in the same letter he enclosed this modified version by Shiseido. I have therefore incorporated these modified parts. Matsuzawa had not received any notice from Fujiki's President, Ken Fujisawa and his lawyer, Jirō Yamane. After sending them my quotations once again in June 1999, this time directly, they both responded quickly by letter and approved completely of my quotations, while adding some recent facts in their letters which have been very useful to me.

## 2
## THE DEVELOPMENT OF THE JAPANESE LUXURY COSMETICS DISTRIBUTION SYSTEM

The current distribution system for luxury cosmetics dates back to the beginning of this century. In this period there was very strong competition between manufacturers and retailers and retail prices were low. The wholesale traders *(tonya)* were very powerful and they dumped cosmetic products on the market.

In order to avoid excessive and destructive price competition Shiseido was the first company to develop its own distribution channel over which it could maintain a great deal of control. In 1924 the first president of Shiseido, Shinzō Fukuhara, established a 'chain-store' sales system[5] to be used for luxury cosmetic brands. This was the origin of the so-called *keiretsu* distribution system[6] within the luxury cosmetics industry. Shiseido started selling its products to selected retailers through newly established subsidiary sales companies. The products were only to be distributed to these retailers at one fixed resale price as determined in the standard-form contracts concluded between the sales companies and the retailers. This turned out to be very successful and many other cosmetics firms followed this example.[7]

Just after World War II there was a second period of excessive competition with low prices, which was backed up by the newly promulgated Anti-monopoly Act which

5 Nikkei Ryūtsū Shinbun (ed) (1993), *Ryūtsū gendaishi* (The Modern History of the Distribution), p. 119–120.

6 There are two main types of *keiretsu:* enterprise *keiretsu* and distribution *keiretsu.* Distribution *keiretsu* consist of numerous wholesale and retail outlets that sell the products of a single manufacturer on an exclusive or semi-exclusive basis. They usually become integrated by various ties and links. See Roy Larke (1994), *Japanese Retailing,* p. 83.

prohibited resale price maintenance. However, a second amendment of the Act in 1953 substantially changed many parts of the Act.[8] For example, under the amended Act the FTC was authorised to designate many commodities as exempt from the general resale price restrictions, including cosmetics. This was to prevent price dumping of brand name goods which would harm medium and small-sized retailers. There had also been pressure upon the government from the industry itself.[9]

This new system gave the manufacturers of cosmetics the right to enforce specific resale prices. In the same year the manufacturers had to notify their price fixing distribution agreements to the FTC. Manufacturers, which had established their own distribution system very much profited from this revision. It greatly enhanced the establishment of distribution systems in which luxury cosmetic products or so-called 'system products' *(seidohin)* were distributed through small stores. These cosmetics gained a larger share in comparison to cheaper cosmetics, which were sold through other channels. Larger retailers, which had the power to sell at a discount, were omitted from the system, making way for small 'mom and pop' selected retail stores.[10]

Manufacturers of luxury brands such as Shiseido, Kanebo, Kosé, Kao, Max Factor, Revlon and Albion gained the upper hand leading to an oligopoly situation with a few manufacturers holding the majority of the market share.[11] These companies had first concluded contracts with their sales companies, each covering its own region. The sales companies in turn concluded more detailed standard-form contracts with their retailers. The luxury cosmetics could only be sold at shops, which had concluded a standard-form agreement with the manufacturer's sales companies. Within this system manufacturers could easily dictate prices to the retailers and prices were high. The prevalence of price fixing in this industry is explained by the fact that compared to other industries, the distribution system of cosmetics is less complex and cosmetics manufacturers have more power to make distributors abide by their marketing policies.[12]

However, in 1971 a women's consumer movement emerged which criticised the resale price maintenance system. They blamed it for the high prices of luxury cosmetics. They sent open letters with questions to the leading manufacturers and urged the FTC to change the resale price maintenance system. The top manufacturer, Shiseido, became the target

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7See Motoshige Itō (1995), *Nihon no bukka naze takai no ka* (Why are Prices in Japan so Expensive?), p. 201–203.

8 Generally speaking, the amendment may have been triggered by the fact that after the Korean War had ended many Japanese industries, which had increased their production capacities in order to meet the large war demands, found themselves with capacities far greater than the market's requirements. A recession followed and in order to restore the economy many businessmen felt that a greater degree of mutual business co-operation was necessary than was allowed under the Act.

9 See M.Itō (1995), o. c., p. 204; Nikkei Ryūtsū Shinbun (ed) (1993), o. c., p. 125–126; Ken Fujisawa refers to the fact that the President of Shiseido at that time, Mr Matsumoto, was also a member of the House of Councilors. See K.Fujisawa (1996), *Shiseido o kokuhatsu suru* (Accusing Shiseido), p. 26.

10 See Yoshio Yamaoka (1990), *Keshōhin gyōkai* (The Cosmetics Industry), p. 137–139; and M.Itō (1995), o. c., p. 204.

for boycotts by this movement. The FTC started to investigate the cosmetics industry and eventually in 1974 the FTC reduced the number of cosmetics designated as exempt from the general resale price restriction to 24 cosmetic products which are sold at a price of 1, 030 Yen or less.[13]

Accordingly, several manufacturers changed or drafted new standard-form distribution agreements and showed it to the FTC for approval. For example, Shiseido drafted a 'Shiseido Chain-Store Contract' in 1974 and renewed contracts with its distributors. This new standard-form agreement was shown to and unofficially approved by the FTC. It was drafted in the Corporate Relations Department *(hanbai chōsabu)* of the Shiseido head company.[14] At the beginning of the 1990s the FTC further investigated the resale price maintenance system and in April 1993 once again reduced the number of designated cosmetics from 24 to 11.15 In April 1997 the last 11 articles were finally removed from the list, which meant that all exemptions were abolished.[16]

### *The Trade Relationship between the Sales Companies and Retailers*

This distribution system for luxury 'system goods' was very successful and it became profitable to become a distributor of prominent brand-name products. Such distributors received all kinds of assistance from each manufacturer in relation to the sales of their products.

Most of the retailers concluded contracts with three to four manufacturers. At the end of the 1980s Shiseido had a contractual relationship with some 25,000 retailers, Kanebo with 22,000, Max Factor with 15,000, Kosé with 10,000, Kao with 10,000 and Albion with 8,000 stores.[17] Through various business practices and duties imposed on the distributors each manufacturer exerted control over the retailers and maintained its strong brand recognition. The contracts concluded between sales companies and retailers were standard-form and brief, with on average only around 20 articles. This can be contrasted

11 In 1996 they held around 65 percent of the market. See *Nikkei Weekly,* 5 August, 1996.

12 Nikkei Ryūtsū Shinbūn (ed) (1993), o. c, p. 126.

13 See Y.Yamaoka (1990), o. c., p. 183–184; and M.Itō, o. c., p. 204; See also *Asahi Shinbun,* 14 October 1994.

14 Takafumi Uchida, Personal communication, 23 May 1994.

15 There had been strong pressure from the LDP, which had established its own committee on this subject, not to move too quickly as regards changes. See *Asahi Shinbun,* 21 December 1993.

16 See for this development of the cosmetics distribution system, M.Itō (1995), o. c., p. 189–230.

17 Y.Yamaoka (1990), o. c., p. 153.

18 In addition manufacturers concluded special contracts with price-fixing clauses for those products which were designated as exempt from the general resale price restriction. Since the entire system has been wound down over the years, these special contracts have also diminished.

with selective distribution agreements in the EU countries such as the Netherlands which are longer and more detailed.[18]

Although these contracts show some variety they share many similarities. In most of them the following duties are imposed upon the retailers in order to make this system very close and tight and to create a relationship of mutual dependency.

First, one important duty is the duty to give proper explanation about the products and to provide after-service to the customers according to the directions of the sales companies.[19] Second, most contracts also impose duties upon the retailers to participate in seminars about management and sales and to keep a register of all customers. Third, under the terms of the contract retailers are obliged to establish special corners in their stores for the products of one manufacturer which are usually designed and paid for by the manufacturers themselves.[20] Over the years up until the present, partly due to the events described below, these contracts have become somewhat more specific in relation to the duties imposed upon the retailers. This concerns, for example, the duty to sell face-to-face with counselling directly to customers and a prohibition on selling by mail order. It must be noted that the contracts still do not stipulate that sales to distributors outside the sales network of the manufacturer are forbidden. This is probably due to the fact that this would violate the Anti-monopoly Act Guidelines and such clauses would already have been omitted after prior consultation with the FTC.[21]

By contrast, in relation to the obligations of the sales companies the contracts only stipulate that they will endeavour to maintain the strong brand recognition of the products. In some of the contracts some important business practices of the manufacturer are set out, which may be viewed as some sort of obligation on the part of the sales companies. However, these practices are only stipulated in a few general terms. This serves to increase the discretionary power of the manufacturers and is a reflection of their stronger bargaining power. It concerns the following two business practices:

First, there is the practice of dispatching trained sales staff from the manufacturer to the retail stores. The dispatched personnel explain to employees and customers the correct use of the products but they also have a very important function to check resale prices.[22] For example, in 1990 Shiseido employed 9,000 of these so-called loan shop assistants, Kanebo 8,000, Kosé and Max Factor 4,000, Revlon 1,000 and Albion 800.[23]

Second, the provision of rebates by the manufacturers to the retail stores which increases their dependence upon the manufacturer. This practice is sometimes set out in the standard-form contracts in very general terms.[24] This system can be used to induce the distributor

19 Both Article 7 of the standard-form 'Shiseido Chain-Store Contract' and Article 8 in the 'Kao Sophina Beauty Plaza Contract' which I received during the interview with Kao on 14 November 1997, read: "… When selling the products, the retailer will give proper explanation and after-service about every product to the consumers based on the directions of the sales company…". Furthermore, Article 9 of the Shiseido chain-store contract reads: 'The chain-store will perform all the policies and all the special measures concerning the sales of the Shiseido products as determined by the sales company".

to co-operate and make it more dependent. Rebates may be interpreted as rewards or as penalties.[25]

Finally, it must be noted that there are no stipulations in the contract which restrict the freedom to choose a trading partner. This is in contrast to many selective distribution contracts in the EU, which provide for detailed selection procedures for distributors which demand admittance to the sales network.

In relation to the termination of the contract, all manufacturers protect themselves with short-term contracts concluded for one year being automatically renewable for one further year, unless one of the parties to the contract gives notice of an intention to terminate prior to the expiry of the one-year term. Furthermore, several provisions in the standard-form distribution contracts enable the manufacturers to limit supplies, to stop preferential treatment or even to terminate the agreement when the distributor has breached contractual terms and has not rectified the breach within a reasonable period. In addition, all standard-form contracts include a 'notice at any time' termination clause. Both parties may cancel the contract intermediately with at least 30 days' notice.

## 3
## SHISEIDO V. FUJIKI

### 3.1
### The Relationship between Shiseido and Fujiki before the Cancellation

Shiseido is the largest cosmetics manufacturer in Japan, mainly selling luxury— cosmetics. Its sale of these products currently comprises 45 percent of the total sales of luxury cosmetics in Japan. In the late 1980s Shiseido had a distribution network which covered 15 sales companies with 105 branches and 25,000 chainstores with which it concluded standard-form 'Shiseido Chain-Store' contracts. On average these chain stores are for 20 percent of their product line dependent on Shiseido products. They purchase the products at 70 percent of the resale prices as indicated by the manufacturer.

In 1962 the Shiseido Tokyo sales company concluded a chain-store contract with Fujiki, a small cosmetics shop located in the centre of Tokyo in Senzoku, Taitō Ward *(Shitamachi)*.

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20 Y.Yamaoka (1990), o. c., p. 97–99.

21 See Masahiro Murakami (1997), *Dokusen kinshihō kenkyū* (A Study of the Anti-monopoly Act), p. 129–130.

22 Generally speaking, sending one's own personnel to trading partners or related institutions is a very common practice within Japanese society. This is done in order to obtain the necessary information.

23 See Y.Yamaoka (1990), o. c., p. 98.

24 For example, in the Shiseido Chain-Store contract which I received on 23 May 1994 during the interview with Shiseido, Article 2(1) reads: *"tō hanbai kaisha wa tō cheinsutoā no keiei kōjō o hakaru tame ni shōshū moshikuwa enjikitei mata wa yūtai tokuten sono ta no hanbai kōzōshin no tame no sho shisaku no*

This shop dates back to more than 120 years. It was established in the Meiji Period (1876) by an ex-samurai from the famous Tokugawa clan, which were former retainers of the Shōgun *(Hatamoto)*. The current director, Ken Fujisawa, is a fifth generation descendent of the founder. Just after World War II the shop not only sold its products over the counter but also started to send the products directly to each customer either at home or at work, all at a 20 percent discount. These so-called 'office sales' *(shokuiki hanbai)* which were aimed at corporations with large numbers of women on their staff, turned out to be very successful. Higher volumes of sales, resulting from this sales method, enabled it to provide a 20 percent discount to its customers.[26]

In order to maintain its name as a cosmetics shop Fujiki decided to start trading with the large manufacturers of luxury cosmetics, which were increasing their market share at a rapid pace. After concluding a distribution agreement with the Shiseido Tokyo sales company Fujiki resold the cosmetics with 'office sales' at a discount of 20 percent.[27]

At the beginning the trade relationship between the Shiseido Tokyo sales company and Fujiki did not differ very much from the relationship of the sales company with the other retail stores. The contract was automatically renewed each year based on a renewal clause in the contract. Fujiki ordered cosmetics by fax, phone and on-line computer and received the supplies usually after one day. Payments were made at fixed times from the 20th of each month to the 5th of the following month. Once a week sales staff from the Shiseido head company were dispatched to the Fujiki store to educate the store's sales staff and to provide counselling directly to customers. Fujiki's dependency upon Shiseido was strong. Shiseido cosmetics were its most important products covering more than 20 percent of the total goods which Fujiki resold and they were very important for its corporate image. Moreover, Fujiki could only obtain Shiseido products from the Shiseido Tokyo sales company. No other channels were available by which to obtain these cosmetics.

However, from the very beginning various sales managers from the Shiseido Tokyo sales company visited Fujiki almost every week and told him to stop the sales at a discount. Neither Noboru Fujisawa nor his son, Ken Fujisawa, who entered the company in 1973 and succeeded his father as director in 1985, gave in to this pressure. Eventually the sales company tried to put pressure on them by other means. It restricted supplies of stock to Fujiki or delivered smaller amounts than ordered. It sometimes even refused to provide samples and gifts which were to be given to Fujiki's customers. Furthermore, Fujiki did not receive any newly established Shiseido brands.[28]

Still, Ken Fujisawa maintained his resistance. He was influenced by his father whose independent lifestyle he had much admired. His father had told him that everybody has to

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*jisshi ni tsutomemasu"*. (In order to work for the improvement of the management of the chain-store, the sales company will endeavour to carry out all kinds of policies such as rewards or support and preferential treatment in order to increase the amount of sales by the chain-store).

25 See Ejiri Hiroshi (1990), *'Nihon ni okeru shōtorihiki keitai no ruikei to tokusei'* (Types and Characteristics of Commercial Trade Patterns in Japan), 950 *Jurisuto* 50–56.

make his own individual decisions in life and remain independently minded. He shared his father's conviction that retailers must be free to determine their own retail prices.[29]

In spite of this pressure, through the efforts of Ken Fujisawa, Fujiki gradually grew much larger than the other chain stores. Fujisawa made the most of his study of Economics at Keiō University and his 3-year experience as a bank employee of Mitsui bank before he entered the company. He had rapidly expanded the sales technique of sending catalogues directly to the offices of his customers and receiving collective orders by phone. It constituted 90 percent of Fujiki's total turnover. Furthermore, Fujisawa's employees had increased from 5 to 70 and by 1990 he had about 100,000 customers around the nation with annual sales of 1.1 billion Yen. The share of Shiseido products was 250 million Yen at its peak.

### 3.2
### The Unilateral Termination of the Chain Store Agreement by Shiseido

Serious problems between Fujiki and Shiseido started after February 1985 when Fujiki had started to use catalogues for its office sales of luxury cosmetics. In these catalogues only the name, price and code of the cosmetic products were laid down. These catalogues were sent to general affairs departments of companies, the women's sections of labour unions, and various corporate clients. They were passed around the offices and customers sent in their orders to Fujiki, usually by fax or by phone. Around December 1987, Shiseido found out that its products were also included in these catalogues and subsequently the Shiseido Tokyo sales company urged Fujiki to remove the Shiseido brands from the catalogues.

In the catalogue which was issued in August 1988 the Shiseido products had been removed, but after Shiseido discovered that Fujiki had put Shiseido products in a separately issued catalogue, on April 12, 1989, Mr Masuda, section-head of the sales department of the Shiseido Tokyo sales company, sent a 'warning for correction' *(zesei kankoku sho)* by registered mail to Ken Fujisawa. In this letter he warned Fujisawa to correct his sales system and stated that he would resort to legal measures based on the contract if Fujisawa would not follow this warning. This letter was checked by the lawyer representing Shiseido, Shūhei Sakurai, a specialist in anti-trust law from the Ishii Law Office in Tokyo, who had already been Shiseido's outside lawyer for 20 years. He became involved in the dispute when this warning was drafted.

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26 Ken Fujisawa (1996), *Shiseido o kokuhatsu suru* (Accusing Shiseido), p. 25.

27 See T.Kuwada (1995), *'Keshōhin hanbai no arikata meguri Shiseido to tatakau Fujisawa Ken'* (Ken Fujisawa's fight with Shiseido concerning the Sales Method of Cosmetics) in: *Nikkei Business,* 23 January 1995, p. 62–64.

28 K.Fujisawa (1996), o. c., p. 30–31; and T.Kuwada, (1995), o. c., p. 64

29 K.Fujisawa (1996). o. c., p. 33–37; T.Kuwada (1995), o. c., p. 64.

The Shiseido Tokyo sales company contended that the chain store had failed to comply with its contractual duties. It argued that under the terms of the contract products must be sold face-to-face and according to the guidance of the Shiseido sales company.

Fujisawa responded that Fujiki had already sold cosmetics with office sales at a discount since 1962 and that neither he nor his father had ever heard any previous complaints about the sales method used. According to Fujisawa, Shiseido only started to express complaints toward Fujiki because Fujiki had become too large and had become a threat to the whole chain-store system. Shiseido had decided to put a stop to the discount challenge.[30] Furthermore, in his view the drafting of the 'warning for correction' was largely influenced by Akira Genma, the current president of Shiseido, who at that time had just been promoted to head of the department in the main company supervising all the chain stores *(cheinten buchō).* Before this promotion he was head of the Shiseido branch office in Italy where he had been able to stop the discounting of Shiseido products by cancelling contracts with discounters.[31]

Ken Fujisawa considered this 'warning for correction' as a last warning, all the more so after he heard that Shiseido had started to make use of a lawyer.[32] He was worried and sought help. Through a management consultant acquaintance he received the name of Jirō Yamane, a lawyer, operating on his own in his office in Matsumoto city. This consultant had told him that if he decided to take on such a large company as Shiseido a legal skirmish would not be sufficient. He would need the assistance of a lawyer who would be prepared to engage in an all-out battle. He said that since there are no lawyers in Tokyo who are able to fight Shiseido he advised him to choose Yamane in Matsumoto city whom he knew for his fighting spirit and previous battles against the Japanese power elites.[33]

The following day they both went to Matsumoto and after listening for 20 minutes to Fujisawa's story, Yamane told him he understood the whole situation.[34] Fujisawa decided to call in Yamane as his attorney because he also believed Yamane was able to challenge Shiseido. He did not choose one of the 7,000 lawyers operating in Tokyo because he had read in the newspapers that there are many cases in which they listen to the arguments of such large companies and advise their clients to give in to their demands.[35]

Both Yamane and Fujisawa were determined to commence battle and felt that they had to fight as a 'samurai' not as a trader. Fujisawa saw it as a fight of some-one with faith in justice *(seigi),* a fight in which one has to strongly take a stand. He felt his life would change from now on and that he would not only live as a trader but also as a warrior. It would be a fight for 'social justice', not only for his own store but also for his customers and Japanese consumers in general.[36]

Jirō Yamane, who had been a practising lawyer since 1966, did not have any experience of distribution matters but he was known for his strong political views and strong anti-establishment disposition. He had been involved in famous political incidents such as the student riots in the late 1960s. For example, he represented the students who had occupied

30 K.Fujisawa (1996), o. c., p. 29; and *Tokyo Business Today,* May 1994, p. 11.

the Yasuda Hall of Tokyo University in 1969 *(Tōdai Yasuda jiken)*. Furthermore, he had taken up many pollution cases. After leaving Tokyo and establishing his office in Matsumoto city he had successfully battled against seven leading manufacturers of spike tires. This had contributed to the enactment of new legislation in which the manufacturing of spike tires was prohibited. Yamane had also started taking on the Ministry of Construction with a civil suit in order to prevent the construction of new dams.[37]

The lawyers of both parties met seven times before reaching an agreement on September 19, 1989, drafting a 'mutual agreement form' *(gōisho)*. The final negotiation session, which took place one week before reaching this agreement, was recorded by Fujisawa on tape. In this session the lawyers of both sides, Ken Fujisawa and the sales representative of the Shiseido sales company were present.

As in prior sessions Jirō Yamane warned Shiseido of the consequences in case the contract would be terminated. He contended that it would amount to a violation of the Anti-monopoly Act. He threatened to report Shiseido to the FTC and at the same time bring a civil suit against the company. He warned that he would present this as a serious societal problem while informing the mass media. This would lead to negative publicity for Shiseido among Japanese consumers. Furthermore, he referred to the recent results of the Structural Impediment Initiative talks between the US and Japan and told Shiseido that its distribution system would be under pressure.[38]

According to Yamane, these threats and the fact that Shūhei Sakurai knew what kind of lawyer he was had a great deal of effect on the length of the negotiations and the final contents of the mutual agreement form.[39] In this agreement it was stipulated that Fujiki would from now on not include Shiseido products in its catalogue and would not sell any Shiseido products based on already issued catalogues. In case Fujiki violated these provisions Shiseido would have the right to cancel the distribution agreement. Furthermore, the mutual agreement form provided that from now on Fujiki would sell the Shiseido products in a way that would conform to all the clauses in the standard-form chain-store contract.

However, according to Fujisawa, it was not expressly stipulated that the 'office sales' themselves were prohibited. In this way Shiseido had given in to some extent to the pressure of Jirō Yamane.[40] According to Fujisawa he was right to believe that sending Shiseido products after orders by phone or fax by existing customers could be continued even without using catalogues.[41] This was even confirmed by a Shiseido statement which Fujisawa had recorded on tape.

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31 Ken Fujisawa, Personal communication 12 November 1997.

32 Ibid.

33 Jirō Yamane, Personal communication, 10 November 1997.

34 K.Fujisawa (1996), o. c., p. 93.

35 Ken Fujisawa, Personal communication, 12 November 1997.

36 K.Fujisawa (1996), o. c., p. 93–94.

After this agreement Fujiki once again omitted the Shiseido cosmetics from the catalogues, but continued to sell Shiseido cosmetics by delivery after orders by phone or fax. Accordingly, Shiseido discovered that the amount of purchases of Shiseido cosmetics by Fujiki had not diminished after the conclusion of the mutual agreement form and found evidence that Fujisawa had sold Shiseido cosmetics by delivery in Aomori in the north of Japan. In response, the Shiseido Tokyo sales company reduced its deliveries. It justified these reductions by arguing that since the conclusion of the mutual agreement form the amount of purchases by Fujiki should have been less than before.

Thereupon, during the many visits by sales managers of the sales company, some of which were recorded on tape by Fujisawa, the demands upon Fujiki increased. First, these managers informed that unless all the people directly involved in sales would attend seminars, deliveries would be stopped. However, only Ken Fujisawa and his wife attended. In addition, they requested Fujiki to register its customers in the special Shiseido customer club *(hanatsubaki),* which Fujisawa rejected.[42]

The relationship deteriorated further when Shiseido wanted to shift its deliveries from the Fujiki's office in Asakusa, Taitō Ward to its shop in Senzoku, Taitō Ward, fearing that Shiseido products were still being sold by catalogue from the office together with other cosmetics. Fujiki rejected this change of delivery, but from January 1990 onwards Shiseido only delivered to that shop. Subsequently, Shiseido asked Fujisawa to pay in cash from then on. Fujisawa agreed but when a Shiseido employee came to collect the money in February, Fujisawa paid with more than 6,000 bills of 1,000 Yen in a large bag.

Meanwhile, according to Fujisawa, Shiseido had on several occasions tried to settle the dispute in a 'business-like' manner by proposing to negotiate as to the amount of money which would be sufficient for Fujisawa to accept the termination of the chain-store contract.[43] When the threat of termination became more imminent Fujisawa informed Shiseido that 'office sales' in themselves were not expressly forbidden by the contract. Shiseido countered by saying that it was a matter of interpretation.[44] According to Fujisawa, Shiseido had once more changed its stance by arguing that the mutual agreement form stipulated that office sales without using catalogues were also prohibited.[45]

Eventually, Shiseido judged that Fujiki did not intend to change its sales method and on April 25, 1990, it sent a notification to Fujiki that the contract would be cancelled. Shiseido left an order for about 510 million Yen unfulfilled. Shiseido cancelled the contract with 30 days' notice, referring to the provision in the contract, which made any intermediate termination after 30 days' notice effective. According to Shiseido it invoked this provision while relying on the principle of freedom of contract.[46]

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37 Jirō Yamane, Personal communication, 10 November 1997.

38 Ibid.

39 Ibid.

40 Ken Fujisawa, Personal communication, 12 November 1997.

41 Ibid.

According to Yamane, there had been much pressure upon Shiseido by many regular chain stores organised in the 'National Cosmetics Retailers Union' *(zenshōren)* to stop supplying cosmetics to Fujiki. He had found evidence of letters written by chain stores to Shiseido containing such a plea.[47]

### 3.3
### Response by Fujiki

Despite the letter of cancellation, Ken Fujisawa did not accept the validity of the termination and continued to order Shiseido cosmetics, which was refused. He maintained that there must be freedom for distributors to sell in the way they see fit and consumers must also be free to purchase in the way they want.[48]

For Fujisawa this was a major loss. He was cut off from one third of his business when the shipment of Shiseido products was finally stopped on May 15, 1990. His reputation was damaged and he also risked being cut off from the luxury cosmetics of other leading manufacturers. Fujisawa and Yamane decided to file a complaint against Shiseido with the FTC on May 22, 1990. They appealed to the FTC to rule that the termination of the contract and the suspension of supplies had violated the Anti-monopoly Act, while invoking the Articles concerning resale price maintenance.[49]

When filing the complaint they had placed their hopes on the increasing US pressure as illustrated in the Structural Impediments Initiative talks and the subsequent promises by Japan to enforce the Anti-monopoly Act more strictly and to strengthen the FTC.[50] One month after filing the complaint with the FTC Yamane and Fujisawa visited the FTC and presented a written request *(mōshiire sho)* directed to the Chairman of the FTC in which they once more urged the FTC to take measures against Shiseido.[51] Immediately after that they held a press conference at the local news section of the reporter's club of MITI. They wanted to make known to the general public how Shiseido maintains its high prices.[52]

The reasons for going public were not only to mobilise public opinion and put pressure on the FTC but also to avoid other manufacturers from cancelling contracts with Fujiki.[53] Next, they sent open letters to the Chairman of the FTC asking questions about the FTC's relationship with a body called the Fair Trade Institute (FTI), which is an external affiliate of the FTC. Fujisawa and Yamane were suspicious of any strong relationship between the FTC and large corporations. They had found out that Seiji Ishino, Chairman of Shiseido, was one of the directors of the FTI.[54] In these open letters they also asked for the names of

42 According to Ken Fujisawa, in the past 28 years Shiseido had never demanded that such a list of customers be shown. The requirement for all his employees to attend seminars at the same time was also unusual. See K.Fujisawa (1996), o. c., p. 54–56.

43 K.Fujisawa (1996), o. c., p. 58–62.

44 Ken Fujisawa, Personal communication, 12 November 1997.

45 Ibid.

46 Hiroshi Kubo, Personal communication, 20 November 1997.

the people who had attended the meetings organised by the FTI in which FTC staff gave lectures on the Anti-monopoly Act. In addition, they asked whether the FTC staff had received money, which went beyond the mere coverage of expenses for the lectures.[55]

Furthermore, Fujisawa had gone to the FTC on a number of occasions to explain the situation. Only once had FTC staff asked him any questions.[56] Meanwhile in July 1990 Shiseido had presented to the FTC a written explanation of its sales concept and the necessity of the face-to-face sales.

Finally, on June 10, 1991, one year after the complaint, Fujisawa received a final reply from the FTC, which consisted of a single message: "We have decided not to take action in this matter". No further explanation was given.[57] One year later in response to the order to investigate which was instigated under the name of Masayo Ōkuma, head of the general affairs section of the Cabinet of the Executive office, the FTC on June 10, 1992, notified that the investigation had been abandoned on May 15 because facts in violation of the Anti-monopoly Act had not been found.[58]

Fujisawa and Yamane's distrust of the FTC became stronger and they decided to turn to civil litigation as a final means by which to fight Shiseido. Yamane thought his chances of success were 10 percent. He had not wished to bring an action at the same time as a complaint before the FTC because he was afraid that in such a case the FTC might remain passive and await the decision of the civil court. Furthermore, since a civil suit takes a very long time it was not his first option.[59]

At first, he applied for a provisional disposition *(karishobun)* at the Tokyo District Court. However, the judge told Fujiki that an application for an injunction to prevent the termination of the agreement would only have a small chance of success and thereafter Fujisawa withdrew the application, arguing that he could not expect a fair decision by the court. Yamane and Fujisawa did not have much faith in the judge. In their opinion judges in *karishobun* proceedings never render any decision if the issue in consideration is complicated and without any precedent.[60]

Subsequently, on 30 October 1991, Fujisawa brought a main action against Shiseido before the same court. He asked the court to declare Shiseido's unilateral termination of the contract invalid and to confirm his contractual rights. He demanded shipments of the

47 Jirō Yamane, Personal communication, 10 November 1997.

48 Kuwada, T. (1995), *'Keshōhin hanbai no arikata meguri Shiseido to tatakau Fujisawa Ken'* (Ken Fujisawa's fight with Shiseido concerning the Sales Method of Cosmetics) in: *Nikkei Business,* 23 January 1995, p. 64.

49 They invoked Articles 2 and 19 of the Anti-monopoly Act and No. 12 of the general designation.

50 Ken Fujisawa, Personal communication, 12 November 1997.

51 The contents of this request are presented in K.Fujisawa (1990), o. c., p. 95–97.

52 Ibid. p. 95–97.

53 Ken Fujisawa, Personal communication, 12 November 1997.

54 Ishino had spent most of his career at the Ministry of Health and Welfare, which is charged with overseeing the cosmetics industry. After rising to the very top of the Ministry when becoming ad

cosmetics for the period from March 16, 1990 to June 15, 1991. Fujisawa and Yamane decided not to litigate for substitute damages because these would be limited and difficult to define, making little impact on such a large company as Shiseido. Furthermore, they did not want to settle the matter in monetary terms.[61]

Before the Tokyo District Court Fujisawa referred to the long 28-year business relationship with Shiseido and emphasised that a suspension of supplies had enormous repercussions, since he could only obtain the cosmetics from the Shiseido Tokyo sales company. Furthermore, he claimed that his 'office sales' did not necessarily damage the interest of the consumers. Moreover, he collected evidence to prove that the breach of the duty to sell face-to-face was merely a pretext for the sales company to cancel for opportunistic reasons.[62] He claimed that Shiseido's real aim was to prevent the discount sales of its products. He tried to establish that the whole issue of face-to-face sales was a smokescreen by collecting evidence that Shiseido luxury cosmetics were also sold in supermarkets and department stores without any prior explanation to the consumers. Fujisawa had even succeeded in ordering these cosmetics over the phone from Tokyo department stores and even from a sales company of Shiseido without any face-to-face meeting.

Furthermore, he argued that in general no material is given to the cosmetics shops, so the necessary know-how and knowledge about the contents is not sufficiently available in order to give an explanation about the product. In addition he added that Shiseido products are not so dangerous that skin trouble can occur if there has been no prior explanation. In his 28 years of doing business with Shiseido skin trouble had never occurred. However, if such would be the case it is not a problem of explanation but a problem of taking the goods back. In such cases the Ministry of Health and Welfare would revoke its permission to manufacture such goods.

Finally, he said that forcing shops to give explanations constitutes a constraint on customers who already know a product after having tried it several times before. During one of the trial sessions Yamane had also questioned one of the witnesses of Shiseido, Mr Masuda, who testified that one day before sending the notification of termination he had visited Fujisawa to enquire about terminating their relationship in a more cordial manner

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miaistrative vice-minister, he 'parachuted' into the Shiseido boardroom by the process of *amakudari* (descent from heaven). See *Tokyo Business Today,* May 1994, p. 12.

55 K.Fujisawa (1996), o. c, p. 126; See also *Asahi Shinbun,* 19 July 1994.

56 Ken Fujisawa, Personal communication, 12 November 1997.

57 K.Fujisawa (1996), o. c., p. 98.

58 As stated in the grounds for *the jōkoku* appeal *(jōkoku riyūsho)* by Jirō Yamane. This was handed to me after my interview with him on 10 November 1997.

59 Jirō Yamane, Personal communication, 10 November 1997.

60 Ken Fujisawa, Personal communication, 12 November 1997.

without the need to resort to legal proceedings. He testified that at that time he had thought about settling the matter in monetary terms.[63]

Shiseido responded by referring to the provision in the contract, which gave it the right to terminate the contract intermediately with 30 days' notice. In addition it presented many reasons which could justify the termination. It argued that it only traded with partners which followed its marketing principles. Under the terms of the contract all Shiseido chain stores are obliged to engage in direct face-to-face sales with their customers in order to explain to each customer individually the correct usage of the products. This was aimed at retaining the good name of the products, preventing skin problems caused by an incorrect application and thus promoting the interest of the customer. Accordingly, Shiseido contended that the acts of Fujiki violated this basic principle, because it sold on a mail-order basis and did not cease to do so even after reaching a mutual agreement in which it had promised to stop selling Shiseido goods in this way.

Meanwhile Shiseido had become more cautious and in 1992 it drafted an 'Anti-monopoly Act Observance Manual' of 60 pages for all its employees. This was based on the Guidelines as promulgated by the FTC in 1991. One section covered the restrictions regarding sales methods. Six pages dealt with resale price maintenance and examples of violations of the Anti-monopoly Act were given. In this section questions were answered about how to deal with chain stores, which started to sell luxury cosmetics on a mail-order basis. On page 29 it stated: "To urge chain-stores to abide by contract terms and to sell face-to-face would not amount to any violation of the Act. However, when shipments are stopped because chain stores do not sell face-to-face this can be considered to be resale price maintenance. Therefore, taking such measures easily should be avoided". The manual also stipulated that any violation of the Act would be closely followed by the media and would damage the credibility and corporate image of Shiseido.[64]

## 4
## KAO V. EGAWAKIKAKU

Almost at the same time a similar termination dispute occurred between a leading manufacturer, Kao, and Egawakikaku, a small discount shop. Kao, currently the sixth largest cosmetics manufacturers with a market share of around 6.5 percent started to sell cosmetics in 1982. It began selling its 'Sophina' brand cosmetics through its sales companies to the retailers.

Kao's sales companies concluded standard-form *'Kao Sophina Beauty Plaza'* contracts with these retailers. This standard-form contract was drawn up in 1982 by the sales and legal department of the head company of Kao. When drafting the contract they looked at the

61 Jirō Yamane, Personal communication, 13 December 1994.

62 See *Tokyo Business Today*, May 1994, p. 11.

63 As stated in the grounds for *the jōkoku* appeal *(jōkoku riyūsho)* by Jirō Yamane.

contracts used by other manufacturers such as Shiseido.[65] For example, one similar clause in the contract stipulated that when selling Kao cosmetic products, the distributor must provide consumers with a proper explanation and after-service while following the directions of the Kao sales company.[66] The relationship with its retailers was similar to those of the other manufacturers with their retailers. However, compared to the contract used by Shiseido it was shorter and imposed fewer duties on the retailers. This standard-form contract was checked informally by the FTC, which altogether took a few days with a few phone calls and visits to the FTC. The FTC gave its approval orally, but only in very vague terms.[67]

On September 2, 1988 the Kao Tōhoku sales company had concluded a standard-form contract with Egawakikaku, a small discount shop located in Sendai city, Wakabayashi Ward. This shop was established in 1980 and started selling cosmetics by way of 'office sales', selling them directly to nurses in hospitals.[68] In addition to sales over the counter, Egawakikaku sold the Sophina brands in bulk, sending them to companies and hospitals based on orders by fax and phone. Egawakikaku started selling the Kao cosmetics at 10 to 20 percent below the manufacturers' recommended retail price which proved to be very successful. The annual turnover of sales of Sophina brands rose from around 900,000 Yen in September 1988 to around 22 million Yen in March 1992. Egawakikaku sold and purchased the equivalent of 100 regular small retailers of Kao.[69] A great deal of the Sophina brands was resold to Fujiki which was never allowed to conclude a contract with Kao. The President of Egawakikaku, Mr Egawa, was a close friend of Fujisawa, the President of Fujiki.

Initially, the relationship was a smooth one and the contract was renewed annually according to the renewal clause in the contract. However, because of the rapid increase of orders the Kao sales company started to suspect that Egawakikaku was reselling its cosmetics in large quantities to discounters such as Fujiki which had not concluded a distribution contract with Kao.

Therefore, salespersons from the Kao Tōhoku sales company often visited Egawakikaku and urged President Egawa to clarify the exact sales routes and the names of the businesses which received Kao cosmetics from Egawakikaku. Furthermore, they repeatedly asked to let their own trained sales staff visit the offices to which these sales were directed.

However, Egawakikaku rejected all these demands. Kao started to cut rebates and eventually demanded that Egawakikaku pay in cash every month. Egawa complied and paid 10 million Yen for the Sophina products every month in cash.[70] Thereupon, Kao started to use the assistance of its outside lawyer when investigating the possibility of cancelling the contract. Meanwhile, Egawa threatened Kao that he would file a complaint with the

64 I received a copy of the relevant section of this manual from Tetsuya Hamabe from MITI when I conducted an interview with him on 14 December 1994.

65 Toshiaki Hideshima from the legal department of Kao, Personal communication, 14 November 1997.

66 This is set out in Article 8 of the standard-form contract which I received after the interview with Kao on 14 November 1997.

FTC if the contract would be cancelled. Finally, even without having proof of 'office sales' and sales to other retailers by Egawakikaku, Kao decided to terminate the contract.[71]

On June 2, 1992, the Kao sales company, by means of registered mail, cancelled the distribution agreement with Egawakikaku by giving 30 day's notice based on the intermediate termination clause in the contract. The sales company did not give any specific reason for the termination. When Egawa asked for the reasons therefor, Kao simply referred to the intermediate termination clause in the standard-form contract.[72] Similar to Shiseido, Kao relied strongly on this termination clause. It believed that relying on the principle of freedom of contract would be better than a termination based on any violation of contractual terms. However, the legal department of the Kao head company consisting of 9 people was anxious about such a termination without providing any reason.[73]

The termination and the halting of Sophina supplies was a major loss for Egawa. He was 30 to 40 percent dependent on Kao cosmetics which he could not obtain anywhere else. He decided to fight back and had enlisted Jirō Yamane, the lawyer who had also represented his friend, Fujisawa. First, Egawa filed a complaint against Kao with the FTC on June 29, 1992. However, when Egawa went to the FTC in Tokyo he was simply told by an FTC official that Kao had not under-taken any resale price maintenance. The official did not listen to his story.[74] Shortly after the complaint Egawa and Yamane decided to bring a main action before the Tokyo District Court against Kao on July 7, 1992. Yamane had lost faith in the FTC and did not want to await its decision as he had done earlier in the case between Shiseido and Fujiki. An application for a provisional disposition was abandoned after the judge told them it would not be successful.[75]

Before the Tokyo District Court Yamane demanded that the court should declare Kao's unilateral termination invalid and to confirm Egawakikaku's contractual rights. Secondly, he called on the court to compel Kao to supply the cosmetics, which had been ordered during the month of June. Yamane contended that the termination was an abuse of rights because Kao's real aim was to prevent the discount sales of its products. Furthermore, Egawakikaku had committed no breach of contract.

Very briefly in one sentence Yamane also mentioned that the termination had violated the Anti-monopoly Act. Finally, he contended that the amount of Kao cosmetics sold constituted 36 percent of the total turnover of Egawakikaku and that Egawa had invested around 19 million Yen in rebuilding the store while relying on the continuation of the contract. Therefore, the termination had a very damaging impact on the retailer.

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67 Toshiaki Hideshima from the legal department of Kao, Personal communication, 14 November 1997.

68 Masao Hirasawa (1997), *'Egawakikaku tai Kao soshō no imi o tou'* (Questioning the Meaning of the Litigation by Egawakikaku against Kao) in: *Kokusai Shōgyō,* March 1997, p. 28.

69 Ibid., p. 30 and p. 35.

70 Ibid., p. 28–29.

71 Yasuyuki Sasayama, Personal communication, 14 November 1997.

Kao countered by arguing first that no valid reason was required for the termination of the contract. In the event that a reason was in fact required Kao pointed to the fact that Egawakikaku had violated contractual terms. Egawakikaku had resold to other businesses which was prohibited in the contract. In addition, it had not resold the products face-to-face although this was required under the terms of the contract. However, this prohibition on reselling to other retailers and the duty to sell face-to-face was not explicitly stipulated in the contract. Yasuyuki Sasayama explained that this might have been caused by the fact that there could have been resistance from the chain stores if these obligations had been strictly forced upon them.[76]

One critic, however, pointed to the fact that only after Egawakikaku had filed suit did Kao discover in an investigation that Egawakikaku had resold to Fujiki.[77]

Meanwhile, Kao had become more cautious. First, in September 1992, shortly after the beginning of the civil suit, Kao added a memorandum *(oboegaki)* to its standard-form contracts. This was checked with the FTC. In this memorandum Kao described in detail the duties imposed upon each store. For example, the stores were obligated to attend seminars, to draft registers of customers and to clarify any sales routes. Most importantly, the duty to sell face-to-face was explicitly laid down. The necessity for this sales method was further emphasised by the duty to install special sales staff in charge of recommending Sophina brands. According to Kao this memorandum did not change the contract but only confirmed and clarified what was already agreed upon. When Kao required each of its stores to sign this memorandum 98 percent agreed. This means that around 100 stores rejected it.[78] Furthermore, in May 1993 Kao drafted an Anti-monopoly Act observance manual for the benefit of its employees.[79]

## 5
## VICTORIES FOR DISCOUNTERS BEFORE THE TOKYO DISTRICT COURT

On 27 September 1993 the Tokyo District Court delivered its verdict in the termination dispute between Shiseido and Fujiki. It ruled completely in favour of Fujiki.[80] The presiding judge, Nobuo Akatsuka, upheld Fujiki's claim that the decision by the Shiseido sales company to suspend shipping products was illegal. The court ordered Shiseido to forward products worth approximately 517 million Yen, which had been on order. The judicial intervention was based on the principle of good faith and the court held that it concerned a continuing contract, which cannot be cancelled by a manufacturer without 'unavoidable reasons'.

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72 M.Hirasawa (1997), o. c., p. 30.

73 Toshiaki Hideshima, Personal communication, 14 November 1997.

74 M.Hirasawa (1997), o. c., p. 30.

75 Jirō Yamane, Personal communication, 10 November 1997.

Furthermore, the court also referred to a violation of the Anti-monopoly Act. It held that although the obligation to carry out face-to-face sales is justifiable if such sales are reasonably necessary to ensure the safety of products, to protect the quality thereof, to maintain the goodwill of products or to fulfil any other appropriate objectives, it was not proven that the face-to-face sales method required by the manufacturer was designed to accomplish such goals. Rather, the court found that such face-to-face sales helped to discourage distributors from discounting the price of the products and assisted in maintaining the manufacturer's suggested retail price. Consequently the Court concluded that the obligation to carry out the face-to-face sales violated the 'spirit' of the Anti-monopoly Act and, therefore, the termination of the contract by the manufacturer was not justifiable and was therefore null and void. These statements by the court were very similar to the section on the restriction of sales methods in the Guidelines of 1991.

This decision came as something of a bombshell. For Shiseido it was a great shock. It had not expected that the Tokyo District Court would refer to the Anti-monopoly Act, since Fujiki had not really invoked the Act as such.[81] Japanese judges may add legal grounds *ex officio* in their decisions but since there were so few precedents of cases in which the civil courts had applied the Act in termination disputes, for Shiseido it probably came as something of a surprise.

Shiseido immediately appealed against the verdict to the Tokyo High Court on 8 October 1993, arguing that the decision did not recognise the face-to-face sales system whereby trained sales staff from Shiseido and other cosmetics companies teach consumers how to use the products correctly. It also increased the number of lawyers to work on the appeal. The decision also caused great disquiet among the other leading Japanese cosmetics manufacturers, which enjoyed much control over retail prices. This decision gained a great deal of interest in the media. Fujisawa and Yamane held a press conference at the courthouse reporter's club immediately after the decision. A victory for a small shop over the nation's leading cosmetics manufacturer was big news. In general, the Japanese media were positive about this decision, viewing it as a victory for consumers. They predicted a cut in the prices of luxury cosmetic products.[82]

This decision also received much interest from a large number of legal scholars and lawyers who commented on this decision in legal journals. They were divided but many of the better-known scholars were very critical of this decision. They criticised the easy conclusion of the court that an act leading to price stability immediately corresponds to

76 Yasuyuki Sasayama, Personal communication, 14 November 1997.

77 See M.Hirasawa (1997), o. c., p. 31.

78 Mr Nakanō, Personal communication, 14 November 1997. I received a copy of this memorandum from Mitsuo Matsuzawa in December 1994.

79 I received a copy of the relevant section (p. 9–12) during my interview with Kao on 14 November 1997.

80 *Shiseido v.Fujikihonten,* 1474 *Hanrei Jihō* 25 (Tokyo District Court, 27 September 1993).

resale price maintenance. One of the more outspoken articles, which was published a few months after this decision, came from a well-known practising attorney, Kenji Kawagoe, who found that court's interference in the contract had been too extensive. It is not the function of the state to judge whether a certain sales method is reasonable. Such a judgement should be left to the market and the parties themselves.[83]

Ken Fujisawa was in a much stronger position after the decision of the Tokyo District Court and immediately took the initiative to create a new organisation for discounters which had concluded regular contracts with manufacturers, the 'Association of Cosmetics Discounters' *(keshōhin yasuuriten no kai).* This was done in order to join forces and to make strategic moves in cooperating with each other, with Jirō Yamane as their attorney. In this way members could be protected against unilateral terminations of contracts by manufacturers. Manufacturers would thereby be more fearful of the consequences and would cancel contracts with a member of the Association less easily.[84]

Several members filed complaints with the FTC or threatened to bring a civil suit against manufacturers which cancelled or threatened to cancel contracts. For example, the discounters Egawakikaku, Seiwa, Eyeful and Sanee Medicine filed complaints against cosmetics manufacturer Albion because it had cancelled contracts with them or had threatened to do so.[85] Furthermore, Yamane believed that litigation in itself does not carry much weight if it is not accompanied by other actions such as mobilising consumer groups and public opinion.[86] The association started with five distributors from Tokyo city and from Miyagi and Shizuoka Prefectures, which sold cosmetic products at a discount. Within one year five more distributors from within Tokyo and Chiba Prefecture joined the association. Some members specifically asked Fujisawa not to mention their names as being members of the association, fearing that the manufacturers from whom they obtained their cosmetics would exert pressure.[87]

The friction between the manufacturers and the Association of Cosmetics Discounters increased. Ken Fujisawa even submitted protests to the US trade representative office, hoping that its negotiations would take up his case.[88] He even wrote a letter to the President of the US, Bill Clinton, concerning his case. Furthermore, the association continued to exert pressure on the FTC. On February 17, 1994, they sent an open letter to the FTC in which they claimed that the obligation of face-to-face sales and the prohibition on resales to other retailers were means to control resale prices. Therefore the FTC, which had given its prior consent to these contracts, was also responsible for resale price maintenance.[89]

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81 Hiroshi Kubo, Personal communication, 20 November 1997.

82 For example, *Nihon Keizai Shinbun,* 28 September 1993.

83 See Kenji Kawagoe (1993), *'Hanbai hōhō ni kansuru yakujō to tokuyakuten keiyaku no kaijo'* (Clauses Concerning Sales Methods and the Termination of Distribution Agreements) in: *New Business Law* Vol. 532, p. 6–11, Vol. 533, p. 12–18, Vol. 434, p. 19–22. See for comparable critical reviews, Yoshikazu Kawai (1993), 1035 *Juristo* 122; Jirō Tamura (1995), 1069 *Juristo* 141; Masahiro Murakami (1995), *'Keshōhin ryūtsū o meguru dokusen kinshihō ihan kōi no bunseki'* (Analysis of Violations of the Anti-monopoly Act in relation to Cosmetics Distribution), 577 *New Business Law* 10–12.

At the same time the members of this club demanded an investigation by the District Public Procurator's Office into the alleged adhesion of the FTC with cosmetics business circles. Furthermore, they repeatedly sent open letters to the Chairman of the FTC asking questions about the relationship of the FTC with large corporations and with the Fair Trade Institute (FTI).

Meanwhile, the manufacturers also increased their pressure. For example, on July 8, 1994, Shiseido sent a notification to the chain stores which had become members of the Association of Cosmetics Discounters. In this notification it was stated that resales to distributors, which had not concluded any contract with one of the Shiseido sales companies, constituted a breach of contract and would be sufficient cause for adequate measures to be taken.[90]

On July 18, 1994 almost one year after the decision in favour of Fujiki, the Tokyo District Court ruled for a second time in favour of a discounter, justifying its decision mainly on anti-trust law. Also in this case the discounter had not clearly relied upon a possible violation of the Anti-monopoly Act. The presiding judge, Harada, agreed with Egawakikaku in its case against Kao and ordered the latter to supply goods worth around 12 million Yen to the discounter. He found that the termination was an abuse of rights and therefore invalid.

The court held that Kao had only cancelled the agreement because it suspected that sales were taking place at bargain prices, which is a 'serious' infringement of the Anti-monopoly Act. The court had admitted as evidence a tape-recording by Egawa in which the department head of the Kao sales company had told Egawa to sell at the proper price. It did not interpret the contract in such a way that face-to-face sales were absolutely necessary. Finally, the termination was very detrimental to the plaintiff who could not obtain Kao cosmetics from other suppliers. In addition, Egawakikaku had invested a great deal of money in the trade relationship, believing that it would continue.[91]

This decision also made newspaper headlines and was considered to be a follow up of the District Court decision in the Shiseido/Fujiki dispute. Again a large number of legal academics and practising lawyers commented on this decision.[92] Similar to Shiseido, Kao immediately decided to appeal against this verdict to the Tokyo High Court.

This second victory for a discounter also had a great deal of influence on the contractual behaviour of other manufacturers. For example, on July 16, two days before this decision

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84 K.Fujisawa (1996), o. c., p. 149. However, according to Fujisawa even after this decision some of the members faced contract cancellations by some manufacturers, See *Yomiuri Shinbun* (Evening edition), 14 September 1994.

85 See *Nihon Keizai Shinbun,* 13 July 1994; *Yomiuri Shinbun,* 26 July 1994; *Nihon Keizai Shinbun,* 18 March 1994.

86 Jirō Yamane, Personal communication, 13 December 1994.

87 Ken Fujisawa, Personal communication, 12 November 1997.

88 New York Times, 11 October 1993.

89 Jirō Yamane (1994), *'Kokumin ni mihanasareru ka kōsei torihiki iinkai to Shiseido'* (Have the FTC and Shiseido been Abandoned by the People?), in: *Kokusai Shōgyō,* December 1994, p. 55–56.

an affiliated company of Kosé, Albion, had notified that it would cancel a distribution agreement, by providing one month's notice, with one of its retailers, Eyeful, a member of the Association of Cosmetics Discounters, which had sold Albion cosmetics by means of 'office sales' with 20 percent discounts. Albion reasoned that it had discovered that Eyeful had resold its cosmetics to other discounters. This violated the contract, which stipulated that the products must be sold face-to-face to the consumers. However, after the second court victory by a discounter two days later, and a complaint by Eyeful against Albion to the FTC on July 22,[93] Albion changed its policy and decided not to break off contractual relations with Eyeful and to keep supplying its cosmetics to this discounter.[94]

During the same period as the two court victories by Fujiki and Egawakikaku another termination dispute had started between leading cosmetics manufacturers and a discounter, which had much impact upon the other termination disputes.

## 6
## LEADING COSMETICS MANUFACTURERS V. KAWACHIYA

A third dispute occurred between Shiseido and other leading manufacturers on the one side, and, on the other, one of their retail outlets, Kawachiya, a Tokyo-based discount chain-store which ran eight cosmetics shops in Tokyo and Chiba Prefectures.

Kawachiya had a long history of providing discounts. Yukio Higuchi, the President of Kawachiya, had inherited the family business and started managing supermarkets in the 1960s. Thereafter he started to sell alcoholic beverages at discount prices and turned away from the supermarket business. In addition he started to sell cosmetics. For the sales of cosmetics Higuchi started as a regular retailer and concluded contracts with several cosmetics manufacturers. With Shiseido he had concluded a contract in 1973. The share of Shiseido products in his total turnover amounted to between 30 and 40 percent. He was known for his strong personality and his energy in establishing various new stores.[95]

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90 Jirō Yamane (1994), *'Keshōhin no kakaku kōsoku to kōshuin no jittai'* (The Price Restriction of Cosmetics and the Reality of the FTC), in: *Kokusai Shōgyō,* September 1994, p. 34.

91 *Kao v.Egawakikaku,* 1500 *Hanrei Jihō* 3, (Tokyo District Court, 18 July 1994).

92 For a strongly critical review see Kenji Kawagoe (1994), *'Taimenhanbai no yakujō to dokusen kinshihō'* (Face-to-Face-Sales Clauses and the Anti-monopoly Act), 1053 *Juristo* 53–58. For support see for examale Kazuhiro Tsuchida, *'Keizokuteki kyōkyū keiyaku no kaiyaku to fukōsei na torihiki hōhō'* (The Termination of Continuing Supply Agreements and Unfair Trade Methods), 1063 Juristo 122–124.

93 *Asahi Shinbun,* 23 July 1994..

94 *Nihon Keizai Shinbun,* 25 August 1994..

95 See Chigako Ishiguro (1993), *'Gyakkyō in mōe teika fukitobasu rōharai ni amanjizu ta tenka mo'* (In Adversity Blowing Set Prices Away and Establishing Various Stores) in: *Nikkei Business,* 27 September 1993.

The trouble began after March 1993 when Higuchi publicly announced that he would also start selling cosmetic products at discount prices. He established separate companies to handle the discount sales of cosmetics and on June 9, Kawachiya began offering 25 percent to 30 percent discounts on about 5,000 items produced by six leading cosmetics manufacturers in its eight cosmetics shops. At the same time most leading manufacturers started to exert pressure on Kawachiya.[96] In mid-June, Kao started limiting its supplies to Kawachiya. In response the latter immediately filed a complaint with the FTC against the manufacturer. As a discounter Kawachiya had much experience with filing complaints with the FTC and did not have to call in his outside lawyers to draft the complaint.[97]

One month later in July 1993 the first contract cancellations occurred. Two Shiseido sales companies cancelled their distribution agreement with Kawachiya. Shiseido had carried out an investigation in which it had found that Kawachiya had resold its products to Fujiki.[98] Shiseido contended that these measures were due to contractual violations by Kawachiya. It had resold its goods to other retailers, which was prohibited in the contract. As in the dispute with Fujiki, Shiseido emphasised its marketing policy that luxury Shiseido cosmetics must be sold face-to-face.

Shiseido also based the termination on the intermediate termination clause with 30 days' notice. In addition, Shiseido also paid 4.1 million Yen to cover Kawachiya's lost profits. Another manufacturer, Kanebo, started limiting supplies to Kawachiya and recalled its dispatched trained sales staff.

In response to the cancellation, Kawachiya filed complaints with the FTC against Shiseido and Kanebo in which it contended that the termination or cut in supplies violated the Anti-monopoly Act, accusing the manufacturers of trying to prevent it from selling their cosmetics at discount prices.[99] Yukio Higuchi was very confident because on two earlier occasions he had filed successful complaints to the FTC against companies, which had refused to supply alcoholic drinks and medicines after he had started to sell them at a discount. Twice the FTC had delivered a recommendation decision in which these companies were ordered to supply Kawachiya.[100]

In contrast to the response to the complaints by Fujiki and Egawakikaku, on this occasion the FTC responded quickly. It commenced an extensive investigation and raided three Shiseido sales companies and its affiliated companies on 14 September 1993 on suspicion of violating the Anti-monopoly Act. This was only 13 days before the first Tokyo District Court decision in relation to Shiseido's termination dispute with another discounter, Fujiki. The FTC had also planned to search Shiseido's head office at the same time, but just a few days before the planned raid the head of the FTC investigation bureau called it off, explaining that there had been pressure from above.[101]

96 Yukio Higuchi argued that a Shiseido director had pressurized Kawachiya to stop selling at a discount, promising a 10 million Yen 'monthly sales promotion expenditure', Japan Times, 6 November 1993; Also *Nihon Keizai Shinbun,* 2 August 1993.

97 *Nihon Keizai Shinbun* (Evening edition), 2 August 1993.

The Shiseido head office had continuously contended that it was not responsible for the actions of its sales companies, but just after the decision of the District Court, which was favourable to Fujiki, Kawachiya had also filed a complaint against the head office of Shiseido. It argued that the head office had instructed its sales companies to suspend shipments to the discounter. In November 1993 and once again in March 1994 the FTC raided Shiseido's head office and nine affiliated sales companies for allegedly blocking discount sales of cosmetics. These raids by the FTC generated much publicity in Japan. It was the first time for the FTC to search a major cosmetics manufacturer concerning a suspected violation of the Anti-monopoly Act.

This might have taken place because of the strong current of discounting, which swept the country at that time and the widespread publicity which Kawachiya's case had received in the Japanese media. Furthermore, the election of Morihiro Hosokawa as Prime Minister after 37 years of Liberal Democratic Party (LDP) rule in the summer of 1993 might have been of influence. The President of Fujiki, Fujisawa, went so far as to contend that this was of vital importance because before this election the powerful LDP politician Ryūtarō Hashimoto had been the Minister of Health and Welfare and had protected the cosmetics industry, belonging as he did to the group of politicians who protect one particular industry *(zokugiin).* Hashimoto allegedly had some influence over the FTC.[102]

Meanwhile, Yukio Higuchi was increasingly under pressure. Although he had connections with the Association of Cosmetics Discounters he operated largely by himself, not formally becoming a member of this association. His operations were larger than the other discounters and he used his own outside lawyers and decided his own policy.

Another cosmetics producer, Max Factor, which is a subsidiary of Procter & Gamble, also started limiting shipments to Kawachiya and notified that it would no longer send any trained sales staff to Kawachiya's stores. Thereupon, the discounter also filed a complaint against Max Factor.[103] Some manufacturers also limited rebates which caused Kawachiya to raise prices. Finally, some of them decided to completely cease trading with the discounter. In September 1993 the Kosé Tokyo sales company notified Kawachiya that it would not renew contracts, which would expire by the year's end. In addition, two sales companies of Kanebo notified the discounter in December 1993 that they would not renew the contract which would expire in March 1994.[104]

Not only did the manufacturers exert pressure, but also other retailers, united in the association of Tokyo-based cosmetics retailers and 85 of its member-shops, filed a complaint

98 Takafumi Uchida, Personal communication, 20 November 1997.

99 The complaint was filed on 27 July 1993. See Mayumi Suzuki (1994), *Disukaunto sutoā heisei ryūtsū kakumei* (The Heisei Discount-store Distribution Revolution), p. 117.

100 For example, Kawachiya had successfully filed a complaint against 'Satō Medicine' which had halted supplies of '*Yunkel',* a revitalizing drink, after Kawachiya had sold this product at a discount. In a recommendation decision the FTC demanded that 'Satō Medicine' should supply Kawachiya. See *Nihon Keizai Shinbun,* 11 March 1994.

101 See *Asahi Shinbun* (Evening edition), 21 December 1993.

with the FTC against Kawachiya. They accused the discounter of selling at unfair prices, insisting that it was dumping brand-name cosmetics on the market at 25 to 30 percent below recommended retail prices.[105]

At the beginning of 1994 Kawachiya's situation had deteriorated and it decided also to bring an action before the civil courts. Encouraged by the favourable decision of the Tokyo District Court in the dispute between Shiseido and Fujiki, Higuchi applied for an injunction against two Shiseido sales companies in February 1994. These applications were against the 'Shiseido Eastern Kantō sales company' before the Urawa District Court and against the 'Shiseido Tokyo sales company' before the Tokyo District Court.

In these injunction proceedings he demanded a declaration to confirm his contractual rights and demanded the delivery of the supplies on order. He claimed that the termination was unlawful because there was no valid reason therefor and because it violated the Anti-monopoly Act. He further referred to his earlier complaint before the FTC, but stated that the FTC would probably need more time for a decision. In addition, he doubted whether Shiseido would give in to the FTC in case it would issue a recommendation to Shiseido, which would mean that he would have to wait even longer for his supplies.

In August 1994, Higuchi withdrew the application for an injunction at the Tokyo District Court but he maintained his application at the Urawa District Court. Because of the fact that he was still cut off from all supplies of luxury cosmetics, Higuchi decided to also bring main actions against the manufacturers during the autumn of 1994. Kawachiya brought a main action before two District Courts against the same two Shiseido sales companies, two sales companies of Kanebo and the Tokyo sales company of Kosé, which had all stopped supplying to the discounter. Kawachiya once again demanded legal confirmation that it still had a right to receive the supplies based on the contract and demanded the delivery of the supplies ordered.[106]

On the other hand, because of the two court victories of Fujiki and Egawakikaku and the raids by the FTC on Shiseido, there was much pressure on the cosmetics manufacturers. They not only became more cautious in terminating contracts with discounters,[107] but also decided to change their marketing policies and standard-form contracts. Several manufacturers announced that they would make their contracts more transparent. For example, Kanebo was the first manufacturer to announce that it would change its contracts

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102 Ken Fujisawa, Personal communication, 12 November 1997. In his book he quotes an article in the *Asahi Shinbun* of 21 December 1993 in which it was stated that Hashimoto had regularly exerted pressure on the Chairman of the FTC by phone calls urging him to do something about the discounters which, according to him, were dumping prices. See K.Fujisawa (1996), o. c., p. 130–131.

103 The Japan Times, 15 October 1993.

104 *Asahi Shinbun,* 10 December 1994. See for the cancellations by manufacturers other than Shiseido also: *'Kōsei torihiki iinkai no Kawachiya Egawakikaku no shinsa ga shūryō'* (The Investigations of the FTC in relation to Kawachiya and Egawakikaku have come to an End) in: *Kokusai Shōgyō,* March 1996, p. 32–34.

105 The Japan Times, 28 September 1993.

with all its stores when the contracts would be automatically renewed upon the expiration of the final one-year period. In this new standard-form contract they would make a clearer distinction between cosmetics for which face-to-face sales were required and those for which this was not the case.108

Shiseido announced that it would amend contracts with some of its chain stores in which the obligation of face-to-face sales would be abolished.[109] It changed some of its marketing policies and started to reorganise its distribution system. In March 1994 Shiseido announced that 460 brands of luxury cosmetic products, which hitherto had to be sold face-to-face, were going to be sold on a self-service basis. This would be the first step towards a major reform of sales policies. In the summer of 1994 Shiseido established a new brand name for cosmetics on the market, which was to be sold only face-to-face. In this way it tried to emphasise the importance of this sales method.[110]

## 7
## THE FIRST TOKYO HIGH COURT DECISION IN FAVOUR OF SHISEIDO (SEPTEMBER 1994)

Favourable developments for the discounters were somewhat diminished when on 14 September 1994 the Tokyo High Court overturned the District Court's decision in the dispute between Shiseido and Fujiki. This decision was delivered only one year after the District Court decision, which is considerably shorter than the two or two and half years a High Court usually takes to resolve an appeal.[111] The presiding judge, Kin'ichi Takahashi, had presided over three court sessions without examining any witnesses.

Shiseido had invoked the intermediate termination clause and presented 'unavoidable reasons' for the termination. It also invoked the fact that in 1991 the FTC had concluded that Shiseido had not violated the Anti-monopoly Act after the complaint by Fujiki. During these sessions Shiseido also presented as evidence some articles by legal academics, which were very critical of the initial Tokyo District Court decision.

In his decision Takahashi found that Shiseido had been within its rights to cancel the contract. Fujiki had violated the terms of the contract by selling the cosmetics by mail order. Fujiki's acts amounted to a breakdown of the 'relationship of trust' and the court found that 'unavoidable reasons' existed which justified the termination by Shiseido. Fujiki had continued to sell cosmetics by mail order, even after it had promised to cease doing so.

On the issue of the alleged infringements of the Anti-monopoly Act, the Tokyo High Court found: "It is clear that the requirement of the manufacturer to sell face-to-face leads

106 *Nihon Keizai Shinbun,* 15 September 1994. These cases are currently combined before the Tokyo District Court which still has not yet delivered a decision.

107 Ibid.

108 Two different contracts would be used. One for cheaper 'self-service cosmetics' and one for cosmetics for which face-to-face sales were required. See *Nihon Keizai Shinbun,* 5 December 1993.

109 *Nihon Keizai Shinbun,* 31 December 1993 and 11 March 1994.

to price stability but such an effect in itself does not lead to a violation of the Act. Only when this sales method functions as a means to restrict the prices of retailers can the Act be said to have been violated". The court held that there had not been sufficient evidence to prove such a causal relationship.

First, Shiseido had not cancelled contracts with retailers other than Fujiki, which resold at discount prices. Furthermore, when Shiseido realised in 1987 that Fujiki was selling by means of catalogues it also realised that it resold at discount prices. Nevertheless, it did not immediately stop supplies but demanded that Fujiki adjust its sales system. Shiseido demanded that it should adhere to the sales method as stipulated in the contract, but did not demand that it should stop discounting. Finally, the court held that it was important that after a preliminary investigation, based on a complaint by Fujiki, the FTC had concluded in 1991 that Shiseido had not violated the Anti-monopoly Act.

However, the Court took due consideration that just prior to the warning for correction Shiseido had asked Fujiki to stop discounting and referred to the fact that up until that time Shiseido had never before cancelled the contract intermediately because the retailer's sales method had breached contractual provisions. Furthermore, it held that doubts might be raised about the extent to which face-toface sales were required in actual practice since Shiseido cosmetics were also sold without explanation and even over the phone and by mail order. Accordingly, suspicions may arise as to whether this termination might not have been due to Fujiki's discounts. Nevertheless, the court found that there was insufficient evidence for such an assumption. It held: "Given the developments until the termination and the circumstances described above, it is as yet difficult to conclude that based on only these facts the termination was caused by the discounts of the retailer".

The court argued that although in actual practice face-to-face sales did not always occur this sales method was not meaningless. Many chain stores sell Shiseido brands while giving advice directly to the customers. It concluded that there was a rationale behind selling cosmetics to customers in person given the nature of luxury cosmetics. For example, these products may cause allergies on human skin if applied incorrectly. Furthermore, such requirements are not prohibited when they are necessary or helpful in ensuring the proper sales of the product, product safety and quality control and maintenance of goodwill and if they are imposed in a similar way on all other trading partners. In this way it implicitly referred to what the Guidelines state in relation to No. 13 of the general designation on the restriction on sales methods. Finally, the court held that businesses are free to decide which sales policy or sales method they wish to adopt.[112]

For the presiding judge, Kin'ichi Takahashi,[113] it was the first time in his 37-year career that he had had to consider such a termination dispute in which a distribution agreement

110 *Nihon Keizai Shinbun,* 10 August 1994.

111 According to J.Davis it is estimated that appeal proceedings are conducted in approximately 70 percent of the time it takes to complete the original proceedings. Usually the oral argument and testimony phase of an appeal case is quicker than the proceedings in the court of first instance. See Joseph Davis (1996), *Dispute Resolution in Japan,* p. 68, 324.

had been unilaterally cancelled. He stated that this case was exceptional since a violation of the Anti-monopoly Act is rarely an issue before the civil courts. Furthermore, in these kinds of cases distributors usually claim damages instead of supplies. Takahashi said that he had gathered and read many articles by legal scholars and lawyers about the initial District Court decision, including the articles by Kenji Kawagoe who was very critical of this decision.[114] According to Takahashi, in these kinds of exceptional cases the articles by legal scholars and lawyers have an important role.[115] Accordingly, Takahashi had decided that the Act had not been violated.

Concerning the possible influence of this decision on the still running FTC investigations, he held that this decision would not have much impact because the courts and the FTC are separate entities which cannot bind one another. The FTC is able to conduct detailed investigations whereas the Tokyo High Court is not. Furthermore, he had decided that there was no violation of the Act. If he had decided that the Act had been violated, then this might have had some influence on the FTC.[116]

Takahashi did not propose any settlement in court *(wakai)* since he believed that the facts in this case were not conducive for such a settlement. For example, Fujiki would not honour such a settlement since it was litigating while representing Japanese consumers.[117]

This time the Japanese press published some critical articles on this decision. Few journalists in Japan had expected that the District Court decision would be overturned. Although some legal scholars criticised this decision, while having doubts about the reasonableness of the face-to-face sales method,[118] many of them agreed with the reasoning of the court.[119] The Association of Cosmetics Discounters responded quickly and on 20 September 1994 Fujiki appealed to the Supreme Court. Furthermore, in the newspapers and in one monthly magazine, concentrating on the cosmetics industry *(Kohusai Shōgyō),* Yamane severely criticised this decision by the Tokyo High Court.[120]

He appealed to the Supreme Court on 17 November 1994.[121] In his grounds for appeal Yamane mainly invoked errors in interpreting violations of the Anti-monopoly Act and some procedural errors. He argued that the termination of the contract by Shiseido was done in order to stop discounts and the sales by delivery which violates Article 19 of the Act. He invoked No. 12 of the general designation on resale price maintenance, No. 13 on dealing on unjust restrictive terms and No. 14 on abuse of dominant power. Yamane repeated many arguments, which he had already contended before the lower courts and cited some parts of the District Court decision which had ruled completely in his favour.

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112 *Shiseido v. Fujikihonten,* 1507 *Hanrei Jihō* 43 (Tokyo High Court, 14 September 1994).

113 This judge is currently a notary public. Judges in Japan often end their careers as notary publics.

114 Kin'ichi Takahashi, Personal communication, 26 December 1994.

115 Ibid.

116 Ibid.

117 Ibid.

He even wrote that this decision had been widely covered in the media, even in the New York Times.[122] He held that the extensive coverage of his case was caused by the fact that Shiseido had become the symbol of the closed distribution system in Japan.

Furthermore, he argued that the fact that Shiseido had not taken measures against other retailers which resold at discount prices and had not immediately cancelled the contract after it discovered the discounts does not necessarily lead to the conclusion that there was no intention to cancel the contract in order to stop discounts. He also argued that the recognition that Shiseido had urged Fujiki to stop discounting just before sending the warning for correction in itself constitutes a violation of the Act. Finally, he criticised the court's expression that: "it is as yet difficult to conclude that based on only these facts the termination was caused by the discounts of the retailer". He wondered how such an expression could be used in view of the fact that only three court sessions had been held and that he was denied the possibility of hearing witnesses. Therefore, he argued that this was a procedural error constituting an inexhaustive examination of the facts.

Through publicity the Association of Cosmetics Discounters sought to further mobilise public opinion and consumers to back their demands. They established a link with a new small consumer group which, however, had no links with existing consumer groups. This group was opposed to the High Court decision and had presented a petition to the Chairman of the FTC demanding that it should take tough measures on Shiseido. They also presented a petition to the President of Shiseido, Fukuhara, in which they urged Shiseido to renew supplies to the discounters and to clarify the contents of the products, and also to explain the differences in its products for which prices range from 500 to 50,000 Yen per item.[123]

On December 10, 1994, this consumer group organised a symposium in Tokyo with several discounters. Several journalists were present and Jirō Yamane and the Presidents of Fujiki, Kawachiya, Egawakikaku and Sanee Medicine, spoke of their experiences with the leading cosmetics manufacturers. In very emotional lecturers they explained how Shiseido and other manufacturers put them under pressure with restrictions in supplies and

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118 See for example Kenji Sanekata (1995), *'Taimen setsumei hanbai gimu to saihanbai kakaku iji'* (The Obligation to Sell Face-to-Face and Resale Price Maintenance) in: *Kokusai Shōgyō*. No. 28, No.1. p. 44–46.

119 See for example Kenji Kawagoe (1994), *'Shiseido Tokyo hanbai jiken kōsoshin hanketsu no gaiyō'* (An Outline of the Appeal Decision in the Case Involving the Shiseido Tokyo Sales Company), 555 *New Business Law* 19–24; *Jirō Tamura* (1995), *'Shiseido* Tokyo hanbai jiken kōsai hanketsu' (The High Court Decision in the Case involving the Shiseido Tokyo Sales Company), 1069 *Juristo* 141– 143; Masahiro Murakami (1995), *'Keshōhin ryūtsū o meguru dokusen kinshihō ihan jiken no bunseki'* (Analysis of Violations of the Anti-monopoly Act in relation to Cosmetics Distribution), 577 *New Business Law* 9–14.

120 For example, he criticized the judge for not letting him use any witnesses. See Jirō Yamane (1994) in: *Kokusai Shōgyō,* (September, November and December issue, 1994).

121 This is a *so-called jōkoku* appeal. In contrast to a *kōso* appeal before the High Court in this appeal only questions of law are reviewed. There are three types of legal questions that a re-appellant can ask a higher court to review: errors in interpreting the Constitution; errors in interpreting violations of the law; and significant procedural errors. See also J.Davis (1996), *Dispute Resolution in Japan,* p. 327.

contract cancellations. They further contended that Shiseido had to clarify the contents of its products, wondering why the Ministry of Health and Welfare could give permission to place Shiseido products on the market which were dangerous for consumers if no proper face-to-face sales were carried out. Many contended that large enterprises such as Shiseido were protected by ministry officials and politicians, because of a strong personal overlap between business and government bureaucracy.[124]

## 8
## THE FTC RECOMMENDATION AGAINST SHISEIDO (JUNE 1995)

Within the dispute between Shiseido and Kawachiya the first decision was delivered by the Urawa District Court. On February 17, 1995, Judge Enomoto of the District Court of Urawa ruled in favour of Shiseido and rejected the injunction demanded by Kawachiya. The court found that the termination was lawful because Kawachiya had, since May 1993, systematically and intentionally resold Shiseido cosmetics to other retailers. This violated the contractual terms in which face-to-face sales were required and resales to other retailers were prohibited. Because this breach of contract was intentional and systematic the 'relationship of trust' between the Shiseido sales company and Kawachiya had completely broken down. The court did not decide upon the question whether the obligation to sell face-to-face violated the Anti-monopoly Act or not, but only judged that there was insufficient evidence that the termination of the contract had violated the Act and was therefore invalid.[125] Kawachiya appealed against this decision to the Tokyo High Court.[126]

Kawachiya and all the other discounters' final hopes rested on a recommendation by the FTC which took longer than expected. On June 21, 1995, two years after the complaint, the FTC finally delivered a recommendation against Shiseido. It had focused on acts of resale price maintenance and had found out that Shiseido had concluded secret price fixing contracts with 19 Seikyō stores. This violated the Anti-monopoly Act since the exemption system did not apply to contracts with Seikyō stores.[127]

Furthermore it had discovered proof that Shiseido had dissuaded the largescale retailers Jusco and Daiei from selling its products at bargain prices. This was an infringement of Article 19 of the Anti-monopoly Act. Shiseido had also concluded contracts for the sale of its luxury cosmetics with some large-scale retailers and the resale prices as set by these retailers always have a strong influence on the resale prices as set by the smaller retailers of Shiseido.

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122 New York Times, 11 October 1993.

123 *Nikkei Sangyō Shinbun,* 10 November 1994; *Nihon Keizai Shinbun,* 10 November 1994.

124 Through the introduction of Mitsuo Matsuzawa of the Commercial Law Centre I could attend this symposium which was held in the Skyroom on the 10th Floor of the Ginza Nikkō Hotel. Shiseido was also invited but did not attend.

The facts as set out in the FTC's recommendation were as follows:

First, it had found out that large scale-retailer Jusco had asked approval from Shiseido to sell its luxury cosmetics at bargain prices, which was triggered by the reduction on April 1995 in the number of products designated as exempt from the general resale price restrictions. Shiseido denied approval but after a second request it promised to deliver product samples to Jusco as compensation for refraining from selling at a discount. Jusco yielded to Shiseido because it feared that otherwise it would no longer obtain regular supplies of Shiseido cosmetics.

In addition, the FTC had found out that Shiseido had urged a number of large retailers such as Daiei, not to follow the example of Kawachiya, which had planned to start selling at bargain prices in June 1995. Shiseido rejected a similar request by Daiei to sell at a discount and notified Daiei that it would take measures against Kawachiya. Furthermore, Shiseido promised to assist in sales promotion in order to increase the amount of sales as compensation for not selling at a discount. Daiei also conceded to Shiseido fearing a stop of the regular supplies of Shiseido luxury cosmetics.

Therefore, within the recommendation the FTC urged Shiseido to stop pressurising the large-scale retailers to sell at the price indicated and urged it to abandon the price fixing contracts with the Seikyō stores.

The recommendation, however, did not clarify whether the suspension of the supplies to Kawachiya amounted to a violation of the Act. No mention was made of the halting of supplies to Kawachiya based on the alleged violation of the face-to-face sales clause and the fact that resales were carried out to other retailers.[128]

There have been several speculations about the two-years length of the investigations after Kawachiya's complaint to the FTC. One reason may be that the FTC may have had difficulties in judging contracts, which it had unofficially approved of earlier when the contracts were presented to it for prior approval. Another reason may have been the subtle influence of the Tokyo High Court decision, which was delivered in the middle of the FTC investigations. This decision, which ruled that the requirement of the face-to-face sales did not lead to a violation of the Act, may have created a problem for the FTC.[129] A recommendation that would contradict the Tokyo High Court decision could always be rejected by Shiseido and a hearing procedure could be commenced. Shiseido would then be able to appeal against a hearing decision by the FTC to the same Tokyo High Court. For this reason the FTC may probably have wanted to make doubly sure and needed more time to reconfirm all the material.[130]

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125 *Shiseido v.Kawachiya,* 41 *Shinketsushū* 501 (Urawa District Court, 17 February, 1995). Also in M. Murakami (1995), *'Keshōhin ryūtsū o meguru dokusen kinshihō ihan jiken no bunseki'* (Analysis of Violations of the Anti-monopoly Act in relation to Cosmetics Distribution), 579 *New Business Law* 28–31.

126 The Tokyo High Court has not yet delivered a verdict. The case is still pending.

127 See Article 24 (2) clause 5 of the Anti-monopoly Act. Generally speaking, Article 24 stipulates that the exemption system may not apply to acts of a cooperatives such as Seikyō.

The recommendation came as a shock to all the leading cosmetics manufacturers. Until 3 July Shiseido had time to accept the recommendation but it was flatly rejected. The Senior Managing Director, Akira Genma, denied any price fixing by Shiseido with large retailers, arguing that offering product samples is a normal act of business. He only admitted that price fixing had occurred with Seikyō stores and out of the 500 Seikyō stores with which Shiseido had concluded contracts he immediately banned the contracts with 247 of these stores. Genma made it clear that Shiseido would not accept the recommendation.

Thereupon, on July 26, the FTC issued a complaint against Shiseido and commenced a formal hearing procedure.[131] A long-enduring legal dispute was expected but on October 2, 1995, three days before the commencement of the formal hearing, the President of Shiseido, Fukuhara, applied for a consent decision *(dōi shinketsu).* Shiseido submitted a written statement in which it stated that it admitted the findings and the application of the law stated in the complaint and that it accepted a decision without resorting to further proceedings. It filed a plan containing concrete measures to eliminate the possibility of a violation.

Some analysts believed that Shiseido did not want to become involved in a hearing procedure because in such a procedure, which can take more than 10 years, more facts about its price-fixing practice would become publicly known. This would be detrimental to the corporate image of Shiseido with its consumers.[132] Eventually, on October 30, the FTC issued the consent decision.[133]

Several legal scholars wrote their comments on this decision and pointed to the fact that because the case ended by a consent decision many facts still remained unclear. For example, the decision has not clarified the issue whether the face-to-face sales clause or the prohibition on resales to other retailers violates the Anti-monopoly Act.[134] However, on October 1995, the former Executive Office of the FTC had informally issued examples of its replies to

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128 According to Masahiro Murakami this means that the FTC has concluded that the terminations had not violated the Anti-monopoly Act. See Masahiro Murakami (1995), *'Keshōhin ryūtsū o meguru dokusen kinshihō ihan jiken no bunseki'* (An Analysis of the Violations of the Anti-monopoly Act in relation to Cosmetics Distribution), 581 *New Business Law* 34.

129 The Tokyo High Court had stated: "After the District Court decision in this case the Shiseido Tokyo sales company had halted supplies and cancelled the contract with discounters because there were resales to other retailers". According to Yamane, with this statement the Tokyo High Court also hinted at similar reasons for the termination of the contract by Shiseido with Kawachiya in order to influence the forthcoming FTC decision. See Jirō Yamane (1994), *'Kokumin in mihanasareru ka kōshuin to Shiseido'* (Shiseido and the FTC which have been Abandoned by the People) in: *Kokusai Shōgyō,* December 1994, p. 57.

130 The reason why the FTC shifted all attention to the trading relationships between two Shiseido sales companies and Seikyō stores may be that in this way it could point to clear price fixing contracts and memoranda in order to take measures against Shiseido, without having to refer to the face-to-face sales method. In this way it would not have to deviate from the line of thought in the decision of the Tokyo High Court. See, Yasunari Koide, *'Ashikake sannen no Shiseido v. Kawachiya mondai kō-shuin ga imada shinketsu dekinai riyū'* (The Third Year of the Problems between Shiseido and Kawachiya and the Reasons why the FTC cannot Decide), in: *Shūkan Daiyamondo,* 25 February 1995, p. 12–14.

consultations on unfair trade practices. Within these replies it had made clear that imposing restrictions on resales to retailers which do not have the contractual obligation to sell in a specific method, does not violate the Anti-monopoly Act, as long as the restriction on the said sales method is not in violation of the Act.[135]

The decision of the Tokyo High Court had discouraged the discounters but the recommendation of the FTC and its acceptance by Shiseido was good news. Largescale retailers such as Jusco and Daiei gained confidence and immediately started to sell cosmetic products at a discount. However, this was limited to 'self-service cosmetics' *(serufu shōhiri)* costing around 1000 Yen. It did not have much impact on the sales of the more expensive luxury cosmetics which are still sold face-to-face and comprise 80 percent of the market.[136] Other luxury cosmetics manufacturers which had frictions with discounters were disappointed with Shiseido's decision to give in to the FTC demands. They had expected that Shiseido would continue to fight since an acceptance of the decision by the FTC might have detrimental effects for the manufacturers in the still running legal disputes before civil courts. It might, for example, have influenced the forthcoming decision of the Supreme Court.[137]

Meanwhile, the disputes with the discounters had much impact upon the policies of Shiseido. For example in the same year (1995) it established a legal department. Previously, the people responsible for legal matters had worked within many different departments.[138]

Furthermore, just after the consent decision Shiseido announced that it would change its distribution system. In the spring of 1996 it not only changed its marketing policies towards large-scale retailers but also towards its chain stores. It changed its distribution system for luxury cosmetics, which it had used for 73 years and started using new contracts for newly introduced brands. New brands of luxury cosmetics were introduced on to the market for which special contracts were concluded. In May 1996 Shiseido announced that it would conclude these new contracts with only 7,000 of its 25,000 retailers. These outlets were especially designated as chain stores in which the face-to-face sales system was to be employed. These new contracts were not so different from the existing chain-store contracts.[139] However, in the new contracts more duties are imposed on the retail stores in relation to customer service and the registration of customers. The duty imposed on the sales personnel to follow the sales method as provided in the contract is also more expressly

131 *Nihon Keizai Shinbun,* 4 July 1995.

132 See Jirō Aoki, *'Shiseido Fukuhara shachō no okashita aru yakuin jinji no shippai'* (The Mistakes that the Shiseido President Fukuhara has made in appointing his Staff), in: *Seikai,* January 1996, p. 68–71.

133 For the contents of this decision see *Shinketsushū* No. 41, 30 November 1995; also in: *Kosei Torihiki Tokuhō,* Vol. 1394, 7 December 1995.

134 See Masahiro Murakami (1995), o. c., p. 33–35; Also Mitsuo Matsushita (1997), *'Saikin no dokusen kinshihojō no shinketsurei'* (Recent Decisions involving the Anti-monopoly Act), 610 *New Business Law* 22–26.

135 See 1664 *Hanrei Jihō* 15 (1999). *Fukōsei na torihiki hōhō ni kansuru sōdan jireishū* (Collection of Examples of Consultations on Unfair Trade Practices) October 1995, No. 9.

laid down.[140] Lastly, the new contracts stipulate more clearly that legal measures could be taken against stores, which do not provide one-on-one counselling when selling Shiseido brands.[141]

Another change in policy was the abandonment by Shiseido of the traditional rebate system with its retail stores. It started to give allowances in proportion to the number of customers registered.[142] Finally, in 1996 Shiseido once more renewed its Anti-monopoly Act Observance Manual for its employees. Included were sections on resale price maintenance and the restriction on sales methods with questions and answers.[143]

During the same period other manufacturers such as Kanebo, Kosé, Albion and Max Factor followed Shiseido's example, and revised the contracts with their distributors. In order to stop the threat of discounters the duty to sell face-to-face was more clearly laid down within the new contracts. For example, Kanebo had announced that it would change its contracts in April 1996. Its previous contracts had only stipulated that the distributors shall "conduct beauty consultation...and shall endeavour to satisfy consumers". The manufacturers probably believed that controlling their distributors with such vague contracts would be unwise in view of the FTC's stricter supervision of the sales of cosmetics as illustrated by the recommendation against Shiseido.[144] Similar to the new Shiseido contracts they were all checked informally by the FTC during prior consultation.

Meanwhile, the FTC had not conducted any investigations based on the complaints by Kawachiya and other discounters against the other leading manufacturers of luxury cosmetics. Only after the recommendation against Shiseido in June 1995, did the FTC initiate investigations of the sales managers and other related persons from the various sales companies of the other leading manufacturers. Drawing on the experience of the previous Shiseido investigations the FTC ordered certain persons to appear to give evidence and ordered the sales companies to produce various documentary evidence. For example, it instructed them to submit standard-form contracts and asked questions about the way they

136 *Asahi Shinbun,* 1 August 1997.

137 One reason for Shiseido initially not giving in may have been to prevent the negative influence on the still running cases before the civil courts if Shiseido would have agreed that it had carried out resale price maintenance. See *Nihon Keizai Shinbun,* 4 July 1995.

138 In addition to sending my quotations to Shiseido I also asked them the reason for establishing the legal department in 1995. They informed Mitsuo Matsuzawa that the disputes with the discounters had an influence. However, previously there had also been legal experts who worked within the various departments.

139 See F.Hasegawa (1996), *'Shiseido no shin hatsubai seisaku to dokkinhō to no seigōsei'* (The New Sales Policies of Shiseido and their Conformity with the Anti-monopoly Act) in: *Kokusai Shōgyō,* July 1996, p. 31. During my interview with Shiseido on 20 November 1997, I asked a copy of the six new brand specific contracts, but I was told that these were not yet open to the public.

140 Ibid.

141 See *'Shiseido, sore de mo 'taimen' kyōka'* (Shiseido, Nevertheless the Strengthening of 'Face-to-Face'), in: *Nikkei Business,* 6 May 1996, p. 36–38.

were enforced. Questions were also asked about the developments leading up to the termination of contracts. Furthermore, the FTC wanted to know more about the sales methods and pricing policies of the manufacturers.[145]

However, in January 1996 the FTC declared that no violations of the Anti-monopoly Act had been discovered. One problem for the FTC may have been that most of the previous complaints had been filed during the summer of 1993. Because of a shortage of personnel and lack of funds the FTC initially had to focus its energy on the Shiseido investigations which took almost two years. This meant that since the filing of the complaint and the actual investigation the situation had largely changed which made it more difficult to find concrete evidence of resale price maintenance. For example, the sales companies of Kao and Max Factor had already resumed normal contractual relationships with Kawachiya.[146]

## 9
## THE SECOND TOKYO HIGH COURT DECISION IN FAVOUR OF KAO (JULY 1997)

The Tokyo High Court decision in the termination dispute between Kao and Egawakikaku took much longer than the decision by the same court in the case between Shiseido and Fujiki. The presiding judge Suzuki was very cautious. He presided over 10 court sessions and examined many witnesses. According to Mr Nakanō from Kao it may have been of influence that Jirō Yamane was very keen on due process and had strongly criticised the mere three court sessions by the Tokyo High Court in the case between Shiseido and Fujiki.[147] Yamane had even threatened to file a complaint against the judge himself.[148]

Kao had been very worried about the Tokyo District Court decision which had ruled that it had violated the Anti-monopoly Act. Kao had increased its legal team to six lawyers, including specialists in anti-trust law.[149] During the appeal Kao conducted many investigations and surveys among consumers questioning them as to whether they preferred face-to-face sales when buying luxury cosmetics. Half of all the consumers surveyed wanted face-to-face sales and this result was presented by Kao in court in order to illustrate the necessity of this sales method. Furthermore, it presented the result of a survey among retailers in which it appeared that 80 percent of them sold luxury cosmetics by means of face-to-face sales. Finally, Kao also pointed to the fact that after the complaint by Egawakikaku the FTC had decided not to take any measures against it.[150] In January 1996 both Yamane and Kao had received notice in writing from the FTC in which it had concluded

142 F.Hasegawa (1996), o. c., p. 32.

143 I received this new manual during the interview with Shiseido on 20 November 1997. On page 28 in the section on the restriction on sales methods it stipulates that if the enforcement of the obligation to sell by means of counseling is only limited to discounters it will violate the Anti-monopoly Act.

144 See *Asahi Shinbun,* 1 November 1995.

145 See *Kokusai Shōgyō,* March 1996, p. 34.

that Kao had not violated the Anti-monopoly Act. Kao immediately presented this before the Tokyo High Court as evidence.

In contrast, during the appeal Yamane and Egawa repeated their earlier arguments before the Tokyo District Court, but also claimed that Kao had sent 700 letters to different companies asking them if they conducted business with Egawakikaku. According to Yamane, it had done so in order to make it seem as if Egawakikaku was an unreliable company.[151]

After two years presiding judge Suzuki proposed that a settlement in court *(wakai)* be reached. Both parties agreed and on November 20, 1996 they started negotiations. If such negotiations had proved to be successful, the Tokyo High Court would not have to give a final judgement on the legal validity of the termination of the contract and the reasons given for such cancellation.[152]

However, during the following month, on 13 December, negotiations were broken off. Kao had set three conditions for resuming a trade relationship with Egawakikaku: the validity of the termination would be acknowledged; Egawakikaku would sell the Sophina products directly to the customers and would not sell to other retailers; finally, Egawakikaku would once more conclude a standardform contract with Kao together with the memorandum and would honour all the contractual provisions. By contrast, Egawakikaku demanded the renewal of supplies without the condition that resales to other retailers were prohibited and face-to-face sales were required.[153]

Eventually on 31 July 1997 the Tokyo High Court decided in favour of Kao. In the long and detailed decision the presiding judge Suzuki first decided on issues of contract law. He argued that when putting together the provisions in the distribution agreement it could be concluded that a duty of face-to-face sales and a prohibition on resales to other retailers had been agreed upon. The court stated as a general rule that 'unavoidable reasons' are not a necessary requirement for a valid termination. It held that in view of the principle of freedom of contract a party does not have to give a reason for a termination based on an intermediate termination clause. The termination is only invalid if it violates the principle of good faith, constitutes an abuse of rights or violates public order and good morals because it violates a compulsory law. In this case none of the above were applicable. There had also been no violation of the Anti-monopoly Act as one of these compulsory laws. The court concluded that the obligation for retailers to sell face-to-face did not violate Nos. 12 and 13 of the

146 Ibid., p. 37.

147 Mr Nakanō, Personal communication, 14 November 1997.

148 See Jirō Yamane (1997), *'Dokkinhō o azawarau Kao kōshuin to taiketsu suru'* (Taking on the FTC, the High Court and Kao which ridicule the Anti-monopoly Act), in: *Kokusai Shōgyō,* November 1997, p. 26–27.

149 Ibid.

150 Ibid.

151 Jirō Yamane (1995), *'Shiseido ōdaku no jittai to Kao no giman'* (The Reality of Shiseido's Acceptance and the Deception by Kao) in: *Kokusai Shōgyō,* December 1995, p. 85; Jirō Yamane, Personal communication, 13 December 1994.

general designation. This was based on arguments, which were in part similar to those in the earlier Tokyo High Court decision in the case between Shiseido and Fujiki.

The court argued that the reasons for the face-to-face sales method such as giving an added value of advice and the prevention of skin problems for customers might perhaps not be called objective or universal, but there is still some reasonableness attached to this sales method. Although such a sales method leads to price stability, as long as it is not used as a means to restrict resale prices its relative right or wrong should be entrusted to the free choice of the market. The court held that in this case there was insufficient evidence to conclude that the sales method had been used as a means to restrict resale prices. Furthermore, Kao had concluded contracts with identical clauses with the other distributors. Finally the court found it important that Kao was only the sixth largest manufacturer of cosmetics in Japan and the share of its products was only 3.7 percent of the total cosmetics market. This means that its market control was not so extensive.

This time the court explicitly mentioned that a similar situation existed as that referred to in the Guidelines which state that restrictions on sales methods are allowed as long as they are necessary or helpful in ensuring proper sales of the product, product safety, quality control and maintenance of goodwill and if they are imposed in a similar way on all other trading partners. The court also referred to the decision of the FTC in the complaint by Egawakikaku against Kao. Based on an investigation, the FTC had decided not to take any measures since no violation of the Anti-monopoly Act had been found. Finally, it held that the prohibition on selling to other retailers also did not violate the Act since it was nothing more than a means by which to secure the enforcement of the face-to-face sales method.[154]

In response, Jirō Yamane immediately appealed to the Supreme Court on August 8, 1997. According to Yamane, the FTC notification of January 1996, in which it had concluded that Kao had not violated the Anti-monopoly Act, had a great deal of impact on the final decision.[155] According to him, the timing of the FTC was not a coincidence but was aimed at assisting Kao before the Tokyo High Court.[156]

Meanwhile, the Association of Cosmetics Discounters had diminished in size and the discounters faced increasingly difficult times because the manufacturers did not conclude their new brand-specific contracts with the association's remaining members. Egawakikaku and Fujiki were forced only to sell over the counter in the stores they had established all over the country.[157] However, they found a new tactic to attack the manufacturers. They made sure that they would abide by all contractual terms under the new standard-form contracts, which would prove that the refusal to conclude these contracts was only based on their discount sales. First, Egawakikaku had opened new stores and had demanded that Shiseido, Kanebo and Kosé supply their new brands of cosmetics, but this was refused. Yamane prepared a complaint with the FTC and just before filing it, the Shiseido sales

152 *Nihon Keizai Shinbun,* 14 November 1997.

153 Ibid.

company expressed its intention to conclude contracts with Egawakikaku. However, Kanebo and Kosé still refused.

Therefore, on 30 April 1997, Egawakikaku and an affiliated company, *'Bishinkan',* filed a complaint with the Sendai office of the FTC against the sales companies of Kosé and Kanebo, the Japan Cosmetic Retailers Association *(zenshōren)* and the Miyagi Prefecture Cosmetic Retailers' Association *(kenshōren)*. It was the first time that such a retailers' organisation had been the subject of complaint. Egawa argued that the Cosmetic Retailers Association had refused to trade with the stores. As in earlier complaints the discounters argued that the refusal to trade with them constituted a restriction on resale prices which violates the Anti-monopoly Act.[158] Furthermore, Fujiki had also demanded in writing that Kanebo should conclude the new brand-specific contract with it in June but was refused. In response, Yamane filed a similar complaint against Kanebo on August 8, 1997.

## 10
## THE SUPREME COURT DECISION (DECEMBER 1998)

Finally, on 18 December 1998 the Japanese Supreme Court delivered its decision in the case between Shiseido and Fujiki and between Kao and Egawakikaku.[159] Over four years after the first Tokyo High Court decision in the case between Shiseido and Fujiki and almost one and a half years after its second decision in the case between Kao and Egawakikaku,[160] the five judges of the Petit Bench of the Supreme Court unanimously[161] found in Shiseido's and Kao's favour. The decision entirely involved issues of anti-trust law, since in the grounds for appeal the two discounters had mainly invoked the Anti-monopoly Act. The court dealt with the question whether Article 19 and Article 2(9)iv had been violated by the manufacturers when they cancelled contracts with the discounters.

In the case between Shiseido and Fujiki the Supreme Court considered whether No. 13 of the general designation, which prohibits dealings on unjust restrictive terms, had been violated. The Court first provided the following general rule:

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154 *Kao v.Egawakikaku,* 1624 *Hanrei Jihō* 55 (Tokyo High Court, 31 July 1997). Again the response of the legal academics was divided. For support see for example Hiroshi Iyori (1997), *'Tokuyakuten keiyaku no nin' i kaiyaku ken to hanbai nettowāku shisutemu'* (The Right to Terminate a Distribution Agreement at Will and a System of Network Sales), in: *New Business Law* Vol. 626, p. 17–23 and Vol 627, p. 48–54; and K.Kawagoe (1997), *'Keshōhin hanbai ni okeru tokuyakuten keiyaku no kaiyaku no kahi'* (The Propriety of a Termination of a Distribution Agreement in the Sales of Cosmetics), 625 *New Business Law* 12–14. For a critical review see for example Kazuhiro Tsuchida (1998), *'Hanbai hōhō no gimuzuke to fukōsei na torihiki hōhō'* (Making a Sales Method Obligatory and Unfair Trade Methods), 1128 *Juristo* 115–118.

155 Although the civil courts are not legally bound by FTC measures, whatever their nature may be, these notifications that the Act had not been violated can still have an influence.

156 Jirō Yamane (1997), o. c., p. 28. It was also argued by Hasegawa, who interviewed Yamane in this article, that normally administrative bodies, including the FTC, are very reticent in deciding on issues which are still running before the civil courts., Ibid., p. 28.

157 *Nihon Keizai Shinbun,* 1 August 1997.

> In view of the fact that the freedom of choice as regards the sales policy and the sales method of a manufacturer or wholesaler must be respected, we conclude that as long as the restrictions on the sales method imposed upon the retailers (for example, giving directions about the method of product display and product maintenance and obliging them to give explanations to the customers) are based on reasonable grounds for the sale of such products and as long as similar restrictions are imposed upon the other trading partners, they do not exert a detrimental influence on the fair competition order and therefore do not correspond to dealing on terms which 'unjustly' restrict the business activities of the other party as stipulated in No. 13 of the general designation.

Applied to this case the Court ruled: "The face-to-face sales method is a method of selling cosmetics with the added value of giving explanations of the cosmetics and giving advice to customers about the choice and the manner of application (at least having made complete arrangements to give advice and explanations at all times upon the customers' request). Shiseido adopted this sales policy for reasons of maintaining the confidence of customers in Shiseido products, because this sales policy enables it to satisfy customers by way of complying with their requests. The customers want to increase the beauty effect in applying cosmetics under the best conditions while taking care to prevent skin problems such as rough skin. Therefore, in view of the characteristics of cosmetic products, it is reasonable that Shiseido has adopted the face-to-face sales method. Furthermore, given the fact that Shiseido has concluded similar contract clauses with other trading partners and that in practice a fair number of Shiseido products are sold face-to-face, the obligation to sell face-to-face for Fujiki does not fall under dealing under restrictive terms, as mentioned in No. 13 of the general designation".

The Court also dealt with the question whether No. 12 of the general designation, which prohibits resale price restrictions without proper justification, had been violated. It held that when the restrictions on sales methods function as a means to restrict resale prices, such sales methods might violate the Anti-monopoly Act. However, the court reiterated that which had been held by the Tokyo High Court in arguing that restrictions on sales methods may indeed lead to an increase in sales expenditures and price stability, but that such an effect in itself does not immediately signify that the freedom to set resale prices is thereby restricted. Finally, the Supreme Court did not agree with Yamane's argument

158 *Nikkei Sangyō Shinbun,* 1 May 1997.

159 *Shiseido v. Fujikihonten,* 1664 *Hanrei Jihō* 3, *Kao v. Egawakikaku,* 1664 *Hanrei Jihō* 14 (Supreme Court, 18 December 1998).

160 Usually it takes an average of one and a half to two years for decisions to be rendered. See J.Davis (1996), o. c., p. 330.

161 The Supreme Court's benches are the only courts in Japan where all the decisions do not have to be unanimous. In some appeals there may be separate concurring or dissenting opinions. See J.Davis, Ibid., p. 329

concerning procedural errors. In relation to any further grounds for appeal as put forward by Yamane the court accepted the factual finding of the Tokyo High Court and concluded that based on these facts there had been no violation of the principle of good faith or abuse of rights. Yamane's criticism of the collection of evidence by the Tokyo High Court was viewed as a simple criticism of the factual finding by the High Court or a personal opinion and was therefore not adopted.

In relation to the case between Kao and Egawakikaku the Supreme Court used identical arguments to conclude that both Nos. 12 and 13 of the general designation had not been violated. However, it also dealt with the question whether the prohibition on reselling to other retailers violates the Anti-monopoly Act. The Court found that "if cosmetics are being resold to retailers which have not concluded distribution agreements and which are not obliged to sell face-to-face, the purpose of the distribution agreement to maintain the brand image of the Kao cosmetics, can no longer be realised. Therefore, the prohibition on sales to retailers with which Kao has not concluded this agreement must inevitably go together with a duty to sell face-to-face. In case the face-to-face sales clause is not held to violate Article 19 of this Act, automatically such a prohibition does therefore also not contravene this Article.[162]

This decision was not as widely covered by the Japanese media as the previous decisions in these cases. The major newspapers only published brief articles thereon.[163] Legal scholars were divided. Well-known legal scholars such as Hiroshi Iyori and Masahiro Murakami strongly supported this decision because it respects the freedom of manufacturers to adopt their own sales policies. They both believed that this decision would have a great impact upon Japanese distribution agreements and distribution systems. Particularly for the distribution of brand name products, where the duty to sell face-to-face is often imposed. Furthermore, it has a great deal of influence upon other industries such as the electronics and pharmaceutical industry, where similar obligations of providing service are imposed upon the retailers within standard-form distribution agreements. This decision may also have much impact upon franchise systems.[164]

However, as before some legal scholars have doubts about the reasonableness of the face-to-face sales and argue that the options for retailers to choose their own sales methods are very limited. Therefore, competition is restricted which necessitates an intervention by the Anti-monopoly Act in order to define the 'reasonableness' of the sales method.[165]

The Guidelines obviously had a great deal of influence upon the decisions from the various civil courts. However, at the same time this illustrates the ambiguity of the expressions used within the Guidelines, since the District Courts reached different conclusions than the High Courts and the Supreme Court.[166] It is furthermore interesting to note that to some extent the Supreme Court decision may have been contradictory to the Guidelines.[167] According to legal scholar Masahiro Murakami a further explanation of No. 13 of the general

162 *Kao v. Egawakikaku,* 1664 *Hanrei Jihō* 14 (Supreme Court, 18 December 1998).

designation was first provided by the FTC Guidelines but ultimately by case law. Because of this decision case law on the restriction on sales methods and customers is settled and the sections of the Guidelines, which contravene the decision, may have lost their validity.

First, the Guidelines stipulate that if the manufacturer's prohibition on selling among distributors is carried out in order to prevent resales of its product to discounters, and if therefore the price level of the product is likely to be maintained, such prohibition is illegal. However, the Supreme Court held that if the obligation upon distributors to sell face-to-face, as stipulated in the distribution agreement, is based on reasonable grounds, the prohibition on reselling to other retailers which had not concluded these agreements (this may include discounters) does not violate the Act.[168]

Second, the Guidelines frequently stipulate that vertical restrictions are "illegal in case the price level of the product covered by the restriction is likely to be maintained". However, as regards the question whether resale prices are restricted or not, the Supreme Court held that "restrictions on the sales method may lead to price stability but that such an effect in itself does not immediately signify that the freedom to set resale prices is thereby restricted".[169]

For the cosmetics discounters the situation has become much more difficult in recent years. For example, Max Factor has recently informed Fujisawa that it would reduce its supplies to Fujiki to ten percent of the usual amount.[170] According to Fujisawa, the manufacturers of luxury cosmetics still try to prevent a rise in the number of discount stores and discount products. For example, even if a discounter sells the products face-to-face, the manufacturers endeavour to limit the supplies to these stores by applying brand specific and store specific contracts and imposing upon them a prohibition on opening new stores and selling new brands.[171]

Meanwhile, recently the FTC has finished an investigation into the actual situation of retail sales of cosmetics for which face-to-face sales are required among the four largest cosmetics manufacturers. This investigation was triggered by indications that these cosmetics are often sold at the price indicated by the manufacturers. On 29 June 1999, the results were made public and it turned out that only a few cosmetics retailers continuously offer discounts to the customers.

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163 See for example *Yomiuri Shinbun* and *Asahi Shinbun,* 19 December 1998.

164 See Hiroshi Iyori (1999), *'Keshōhin taimen hanbai jōkō ni kansuru saikōsai no futatsu no hanketsu'* (Both Supreme Court Decisions in relation to the Cosmetics Face-to-face Sales Clauses), 658 *New Business Law* 11–15.; See also Hiroshi Iyori (1999), *'Saikōsai keshōhin no taimen setsumei hanbai o yōnin'* (The Supreme Court Approves of the Face-to-face Sales of Cosmetics), in: *Kokusai Shōgyō,* March 1999, p. 22–27; See also Masahiro Murakami (1999), *'Shiseido Kao jiken saikōsai hanketsu no nokoshita kadai'* (Remaining Issues after the Supreme Court Decisions in the Shiseido and Kao Cases), 667 *New Business Law* 8–9.

165 See Hiroko Nakagawa (1999), *'Keshōhin no taimen hanbai to dokusen kinshihō'* (The Face-to-face Sales of Cosmetics and the Anti-monopoly Act), 1154 *Juristo* 92–98.

166 See H.Iyori (1999), o. c., 658 *New Business Law* 16. See also H.Iyori (1999), in: *Kokusai Shōgyō,* March 1999, p. 28.

167 H.Iyori (1999), Ibid., p. 16–18; See also Masahiro Murakami (1999), o. c., p. 14–15.

For example, among the 122 regular retailers who had responded, only 16 percent offer discounts on a regular basis. Many retailers, including large-scale ones, only temporarily sell face-to-face cosmetics at bargain prices or sell them only to a limited number of customers. The FTC findings also indicated that the large manufacturers do their best to inform all their employees about possible violations of the Anti-monopoly Act, such as interfering in the setting of resale prices. There were only a few examples of managers from sales companies who had complained to retailers which were selling at bargain prices.[172]

## 11
## CONCLUSION

First, it must be noted that these termination disputes are exceptional. Within such distribution systems, in which strong ties and links exist between manufacturers and retailers, it is not common for retail stores to bring a civil case or to file a complaint with the FTC against leading manufacturers after their contracts have been terminated. Furthermore, leading manufacturers such as Shiseido and Kao rarely become involved in litigation within Japan. They usually terminate contracts more amicably giving adequate compensation or adequate notice upon termination, which also prevents distributors from bringing actions before the civil courts. Legal termination disputes are usually initiated against small manufacturers which more readily terminate in an abrupt fashion, giving the distributor no choice but to litigate in order to be compensated for the damage suffered.[173]

In order to understand why these unilateral terminations of contracts by leading manufacturers have led to such major termination disputes it is important to realise that the discounters were larger and more powerful than the other retailers. They had grown rapidly with their new sales methods and discounts and were more able to take on such large manufacturers. It had largely become a power struggle between manufacturers and discounters who had started to undermine their own carefully built distribution systems. This kind of power struggle also occurred in other industries but has rarely led to such

168 Masahiro Murakami explains that this rule is very favourable to the manufacturers because they can freely choose their own distributors. However, from now on it is necessary to investigate to what extent, in cases where the manufacturers' market share is large and competition is impeded, the free will of a manufacturer to choose a distributor can be limited by obliging it to trade with a distributor which is qualified to and wishes to follow the sales method required. See M.Murakami (1999), Ibid.

169 Murakami explains this difference by pointing to the fact that the relevant sections in the Guidelines were laid down without there being any precedents in the form of FTC or court decisions. See M.Murakami (1999), Ibid. However, one Japanese legal scholar argues that the Supreme Court decision does not contravene these sections of the Guidelines. See Hiroko Nakagawa (1999), *'Keshōhin no taimen hanbai to dokusen kinshihō'* (The Face-to-face Sales of Cosmetics and the Anti-monopoly Act), 1154 *Juristo* 93–94.

170 This was notified to me by Jirō Yamane in his letter of 17 June 1999 in which he had given his approval of my quotations.

171 This was notified to me by Ken Fujisawa in his letter of 22 June 1999 in which he had given his approval of my quotations.

extended legal termination disputes. One reason may be that the cosmetics industry is one of the last industries where the prices of luxury products are still almost completely controlled by the manufacturers. However, a comparable termination dispute has occurred in the microelectronics industry, where Matsushita had cancelled a distribution contract with discounter Daiei, which has now become one of the largest retail chains in Japan.[174]

These termination disputes in the cosmetics industry are also exceptional in that some discounters are continuing to fight until the very end. Although they obviously wished to continue their profitable bargain sales, from a business point of view, with such lengthy court procedures, there is no longer very much that may be gained. Fujiki has been cut off from its supplies of Shiseido products since 1990. Fujisawa did not want to settle the dispute by way of compensation and thereby put a stop to litigation because this would betray his customers and the Japanese consumers which he had come to represent. He even explained such a long fight would not have been possible if he would not have enjoyed it to some extent.[175]

So far, he and other discounters have spent an enormous amount of money in all the legal proceedings initiated. Jirō Yamane has even dipped into his own pocket.[176] It is no exaggeration to say that both Yamane and Fujisawa want to restore traditional Japanese society where politics is still more powerful than the economy. They have used the modern idea of the protection of consumers in order to fight the manufacturers, which stand for the modern Japan with more emphasis on economics.

During my interviews with Yamane he also repeatedly mentioned that Japan has lost its once strong character. In a way he can also be considered a *rōnin*[177] because of his independence and his continuous battles against the Japanese power elites. He had left Tokyo and the Tokyo Bar Association and had started an office on his own in Matsumoto. Fujisawa was also very conscious of his samurai background and he attached much importance to values rather than economic profit thinking.

Another distinctive characteristic of these termination disputes is that in addition to contract law discounters have invoked anti-trust law. The discounters adopted two approaches in order to fight the leading manufacturers and to protect themselves against contract terminations. A complaint with the FTC and an action before the civil courts.

It is obvious that the discounters have made use of the discounting boom in Japan at the beginning of the 1990s. In this period there was mounting criticism against the cosmetics industry where prices remained high. Furthermore, there was increasing US pressure to

172 See for the results of this investigation: *'Kaunseringu keshōhin no hanbai jōkyō no chōsa kekka ni tsuite'* (About the Results of the Investigation on the Sales of Counselling Cosmetics). Published on 29 June 1999. To be found in Japanese on the homepage of the FTC: http://www.jftc.admix.go. JP

173 See Kenji Iwaki (1995), *'Kakaku hakai genshō ka no keizokuteki torihiki'* (Continuing Trade and the Phenomenon of Price Destruction), 560 *New Business Law* 10.

174 This well-known termination dispute between Matsushita and Daiei started in 1957. Matsushita had cancelled the contract with Daiei after discovering that it was selling its products at a discount. Only after 30 years did the dispute finally end.

change such distribution systems within Japan. Therefore, the discounters did much to mobilise public opinion.

In 1993, in the middle of the discounting boom, the developments were favourable for the discounters who had initiated legal proceedings. The two exceptional decisions by the Tokyo District Court, which were justified mainly by competition law, are considered to have been influenced by the new tide which was sweeping the country. Furthermore, it is argued by some people that the election of Morihiro Hosokawa as Prime Minister in the summer of 1993, after 38 years of continuous LDP rule, had brought about the tougher stand of the FTC against Shiseido, leading to the raids on the head office.

However, eventually the discounters did not succeed. Two decisions by the Tokyo High Court reversed the decisions of the Tokyo District Court. The latter had stuck more to competition law whereas the Tokyo High Court adhered more to the logic of contract law. Finally, the Supreme Court decision of December 1998 made it clear that Shiseido and Kao had not violated the Anti-monopoly Act. It is therefore highly unlikely that the discounters will enjoy any further victories, since this decision will likely have a great deal of influence upon the still running legal disputes between cosmetics manufacturers and discounters.

Not only the courts but also the legal scholars were divided. Many of the more influential scholars had been very critical of the Tokyo District Court decisions and supported the later decisions by the Tokyo High Court. They argued that any conclusions about the validity of restrictions on sales methods should be decided by the market itself. On the other hand, supporters of the decisions of the Tokyo District Court were in favour of a more active role of the state and the Anti-monopoly Act. Generally speaking, legal doctrine has most influence upon judges and lawyers when it is related to newly implemented laws or specific subjects on which there are no judicial decisions. Up until that time, there had been no judicial precedents on this issue. Obviously, the critical reviews by some of the more well-known scholars on the District Court decisions and their support of the High Court decisions had a great deal of influence.

Some people have argued that Yamane and his Association of Cosmetics Discounters were too aggressive in their attitude towards the FTC. President Higuchi of Kawachiya, who operated independently from this association of cosmetics discounters, initially had more success when the FTC started its raids on Shiseido, because he only fought the manufacturers and not the FTC. However, Higuchi was eventually equally unsuccessful because the FTC only referred to violations of anti-trust law by Shiseido in relation to large retailers which were not involved in these termination disputes.

These case studies also serve to illustrate the contracting behaviour of the leading manufacturers and discounters and the role of contract law in Japan. Manufacturers first

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175 Ken Fujisawa, Personal communication, 12 November 1997.

176 Ibid.

177 A *rōnin* is the term for a samurai without a vassal, which were numerous in the 17th century. They were very independent and had no protection.

tried to keep the disputes out of the legal sphere. Initially, extra-judicial sanctions were attempted to bring the discounters/distributors more into line with their sales policies. Shiseido negotiated for a long period with Fujiki before it finally cancelled the contract. Gradually, the disputes came within the legal sphere and only at the final stage did manufacturers threaten to make use of the termination clauses in the contract. Leading cosmetics manufacturers usually based the termination of the contract on the provision which provides for termination with 30 days' notice at will, relying on the principle of the freedom of contract. Only when they were required to give a good reason for the termination did they point to several duties and prohibitions which, however, were not always explicitly stipulated in the contract.

This means that their standard-form contracts were very important for the cancelling of contracts. These contracts served to maintain control over the distribution structure and the sales methods. The termination clauses were used only as a last resort when other pressures had not worked. In addition, the importance of contracts was also illustrated by the fact that the majority of manufacturers had amended existing contracts or drafted new contracts for newly established brands. Within these new contracts the duty to sell face-to-face was strengthened and made more explicit. This happened after the manufacturers of luxury cosmetics understood that this duty was not in violation of the Act. The Tokyo High Court decisions and the fact that the FTC had not directly mentioned the face-to-face sales in its recommendation may have influenced this notion as far as the manufacturers were concerned. Currently, the drafting of new contracts for new brands with many duties imposed upon the distributor is also occurring in many other industries.[178]

Furthermore, the establishment of new contracts may have served another purpose. Now, manufacturers can conclude these new contracts only with retailers which abide by their trading policies. In this way they can omit the discounters without having to terminate contracts.

By contrast, the discounters did not believe in the principle of the freedom of contract and demanded a good reason for the termination of such a continuing contract. They placed emphasis very much on the fact that it concerned a long-term distribution agreement and focused on their strong dependency on the manufacturer's cosmetics. They were of the opinion that there was no valid reason for termination and appealed to general principles of contract law, such as the doctrine of good faith and abuse of rights. For some discounters such as Fujiki, it became a matter of principle and pride.

However, they were conscious that in actual practice civil litigation is hardly an option since it takes too much time and money. For them, instigating a full civil suit was the final option after they had filed complaints before the FTC and petitioned for an injunction at the civil courts.

In contrast to the manufacturers, which relied mostly on contract law, the discounters were more successful in invoking the Anti-monopoly Act with complaints before the FTC. Some manufacturers did not cancel contracts, or even resumed supplies after an earlier termination, because they were afraid of being accused of violating the Act. Both Tokyo District Court decisions and the recommendation of the FTC against Shiseido had a great

deal of impact upon the manufacturers. They also had very much influence on the drafting of new contracts which were shown to the FTC for approval.

These case studies also illustrate that although case law on the unilateral terminations of distribution agreements and anti-trust law may protect the distributor, in practice, there is much uncertainty of the law and the access to the dispute resolution fora is limited. Less certainty in the law itself results in fewer distributors taking the risk of litigation. This makes the protection in actual practice somewhat limited. Long delays and high litigation costs are large barriers for any required expeditious remedy. The proceedings for a provisional disposition are not very expeditious. These case studies made me realise how difficult it is for litigants to maintain the initiative and to generate clearer rules on contract and anti-trust law issues. The distributors went very far in their fight against the manufacturers before civil courts and the FTC and did so for political not for economic motives. In Japan usually the bureaucracy maintains the initiative and keeps the law rather vague which gives them much discretionary power.[179] This is illustrated by the informal practices of the FTC which were common in these case studies.

Lastly, these termination disputes also serve to illustrate the subtle interplay between decisions of the civil courts and the FTC and the possibilities of private law enforcement of the Anti-monopoly Act. Undoubtedly, the decisions of the FTC and the civil courts influenced each other. The Tokyo High Court referred to earlier decisions by the FTC which held that no violation of the Anti-monopoly Act had occurred. On the other hand, the FTC investigations of Shiseido were probably influenced by the first Tokyo High Court decision, which ruled that there had been no violation of the Act.

However, the FTC remained vague on the essential point, namely whether the face-to-face sales system violated the Act or not. Therefore, any private law enforcement of anti-trust law had become more difficult for the discounters. Furthermore, these cases show the strong influence of the FTC Guidelines upon the civil courts. At the same time, however, the Supreme Court decision may have contravened some sections in the Guidelines on vertical restrictions and made them lose their validity. This only clarifies the important function of the courts as the final decision maker to settle difficult and complicated issues of anti-trust law.

In summary, it can be concluded that anti-trust law and the general principles of contract law became the main impetus for the formal adjustments to the relationships between manufacturers and their retailers. However, it was especially the Anti-monopoly Act which enabled the discounters to challenge such large companies as Shiseido. The disclosure of a possible violation of the Act is feared by many large manufacturers because it causes adverse publicity which may lead to a significant drop in business.

The legal termination disputes between leading manufacturers and the discounters are typical of test cases. A possible violation of the Act can be made public and both complaints before the FTC and litigation can be used to influence public opinion, the political process

178 See *Nihon Ryūtsū Shinbun,* 12 August 1997.

and court decisions. In the Japanese legal system, where access to the courts is difficult, as we have seen in these case studies, parties rely very much on publicity. Reputation is vital in Japanese business and it is the social stigma of the disclosure of wrongdoing that makes law very important. It functions as a substitute for state coercion.[180] For example, after the FTC recommendation, Shiseido did not continue the hearing procedure, probably fearing negative publicity among consumers. Furthermore, the litigation induced the leading manufacturers to change some of their contracts and they became more cautious before terminating contracts with discounters.

179 Generally speaking, the Japanese bureaucracy has more legislative power than the bureaucracy in many Western nations such as the Netherlands.

180 See J.O.Haley (1991), *Authority without Power, Law and the Japanese Paradox,* p. 181–190.

# 5
# Dutch Law and the Unilateral Termination of Distribution Agreements

## 1
## INTRODUCTION

Although distribution systems in the Netherlands may differ from distribution systems in Japan, a characteristic that these systems share in both countries is that in most cases the distributors are in a weaker bargaining position than the manufacturers. Accordingly, unilateral terminations of distribution agreements by manufacturers may cause similar problems for distributors in both countries. It is therefore possible to compare the Dutch legal response to these problems with the Japanese legal response as a comparative illustration. The purpose of this comparison is not to contribute to comparative law itself but to put my findings on Japanese law and practice into perspective.

As in Japan, in Dutch law there is no direct legislative response to the need for the protection of the interest of the distributor and judicial intervention has been the main source of law. This chapter first compares the Dutch contract law applicable to the termination of distributorship agreements with the applicable law in Japan. In addition, applicable EU and national Dutch anti-trust law are described. As in Japan, in some cases they may have an important indirect bearing in termination disputes.

Since law in the books can be a poor indicator of law in action, I have not only limited myself to the study of textbooks and case law but I have also taken an approach along the lines of the sociology of law. Accordingly, I hope to bring my findings in Japan into perspective.

I collected distribution agreements and conducted interviews with three lawyers specialising in distribution agreements.[1] In addition, in the last section of this chapter a study has been made of the application of this law in one particular industry in the Netherlands, the distribution system for luxury cosmetics. For this study I gathered much background information. For example, I conducted interviews with two lawyers who are specialists in relation to this industry and one general director of the Benelux sales company of Christian Dior. I conducted open semi-structured interviews in which I focused upon their experiences in termination disputes. The quotations, which I have used in this chapter, have all been sent to these people for approval. They were approved with only a few adjustments.

## 2
## THE SITUATION IN THE NETHERLANDS

### 2.1
### Termination Disputes

By far the most disputes within the Netherlands in relation to distribution agreements are triggered by unilateral terminations of these contracts. In the Netherlands where the distribution of goods is a primary component of business activity, unilateral terminations of distribution agreements occur regularly. This is against a background in the Netherlands of a growing tendency among Dutch business people to take continuing business relationships less easily for granted. This might be illustrated by an increase in repeated evaluations of the performance of distributors by manufacturers. The co-operation and communication between a manufacturer and a distributor has intensified since the market sets higher standards for the method in which the manufacturer and the distributor provide service to customers. Accordingly, distributors who do not meet the higher expectations set by manufacturers are more easily confronted with the unilateral termination of their distribution agreements.

As in Japan, quite a number of unilateral terminations have sparked legal disputes some of which have ended up in court. These disputes have not necessarily led to final court decisions since many have been settled out of court. Further-more, even if courts have pronounced final judgements, these have often not been reported. Compared to Belgium, Germany and France the number of reported legal termination disputes in the Netherlands is quite limited.[2]

In the Netherlands so far most research has been conducted into the termination of continuing contracts in general,[3] but recently there has been an increase in research which focuses on the termination of distribution agreements. The main purpose of these studies is to meet the demand for more legal certainty in relation to the termination of these agreements.[4]

### 2.2
### Distribution Agreements

As in Japan, there is no codified legal definition of a distribution agreement. Various expressions are used in business circles, in legal discourse and in judicial decisions. In this chapter I use the definition as set out in Chapter 1:

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1 During my work at one of the largest Dutch law firms, Trenité van Doorne, as a part-time employee from March 1996 until October 1998 I had the opportunity to interview three lawyers specializing in distribution agreements.

2 According to a lawyer who is a specialist in this field, H.E.Urlus, in the Netherlands there is only a limited number of lawyers who regularly deal with termination disputes concerning distribution agreements. Personal communication, 12 August 1997.

An agreement whereby one party, the distributor, agrees to purchase and resell in his own name and for his own account products and/or services of a certain company on a continuing basis and agrees to co-operate with the marketing policy of that company. In turn the company, or its importer or higher-level distributor, agrees to sell and supply these products and/or services to the distributor.

As in Japan, it is difficult to draw up clear categories of distribution agreements. Usually a distinction is made between four different categories: an exclusive distribution agreement, an exclusive purchase agreement, a selective distribution agreement and a franchise agreement. In actual practice, however, the distinctions between these categories are not always evident. In the Netherlands many distribution agreements are not put in writing.[5] Frequently, distributors purchase products from a manufacturer for an extended period of time without the existence of any written contract. In practice, the question often arises whether such a relationship constitutes a distribution agreement or not. Particularly smaller manufacturers/suppliers make use of oral contracts.[6] Even if contracts are in writing they are sometimes incomplete, leaving open questions of how and when to terminate and what obligations may arise there from. This evidently causes problems if the agreement is terminated by one of the parties.[7]

Larger suppliers, by contrast, more often use detailed written contracts and usually include provisions, which give them the right to unilaterally terminate the distributorship contract.[8] In most cases the manufacturer/supplier will draft the agreement and the distributor often has no choice but to accept it. When parties negotiate the contract terms it is usually about the length of the notice period but not about the classical grounds, which can justify a termination.[9]

## 3
## DUTCH CONTRACT LAW

### 3.1
### The Dutch Civil Code

#### *Introduction*

There are no specific rules on distribution agreements in Dutch law. The Dutch Civil Code, which regulates various types of continuing contracts, does not include any special

3 See J.F.M.Strijbos (1985), *Opzegging van Duurovereenkomsten* (The Termination of Continuing Contracts) (PhD Thesis, Nijmegen) and G.J.P de Vries (1990), *Opzegging van Obligatoire Overeen komsten* (The Termination of Obligatory Contracts) (PhD Thesis, Amsterdam).

4 See e.g. C.A.M. van de Paverd (1999), *De Opzegging van Distributieovereenkomsten* (The Ter mination of Distribution Agreements), (PhD Thesis, Amsterdam).; See also J.M.Barendrecht and G.R.B.van Peursem (1997), *Distributieovereenkomsten* (Distribution Agreements), p. 145–184.

provisions governing distributorships. Some legal scholars consider legislation to be unnecessary, arguing that the judicial intervention based on the principle of good faith is sufficient to protect the distributor.[10] In the 1980s there were attempts to enact some legislative protection for distributors but this did not receive sufficient support. One of the reasons may be that those attempting to enact legislation mainly consulted representative organizations of the Dutch wholesalers. Many of them—by the nature of their function—have to rely on smaller distributors to distribute their products in the Netherlands. Such wholesalers were not interested in any extra protection for their distributors.[11] Partly because of the Dutch deregulation policy that commenced in the 1980s it is not to be expected that special legislation will be drawn up for distribution agreements or their termination in the future.[12]

This means that the general rules of contract law are applicable as laid down in Chapter 2 of Book 3 and Chapter 5 of Book 6 of the Dutch Civil Code. These general rules of Dutch contract law, which includes the provision that contracts must be executed in good faith, are applicable to distribution agreements.

### *Provisions on the Principle of Good Faith*

Solutions for the problems caused by the termination of distribution agreements are mainly provided by case law and the Dutch courts primarily apply the good faith doctrine when deciding on these termination disputes. This doctrine as laid down in the important Article 6:248 of the Dutch Civil Code, permeates every branch of Dutch patrimonial law.[13] In order to decide on what is reasonable and equitable, some guidelines are provided in Article 3:12 of the Civil Code.[14] This article, an application of the good faith doctrine, is an important factor, which has a strong influence on court decisions. Judges are required to take into account legal opinion currently held in the Netherlands.

The good faith doctrine has three functions. First, all contracts, including distribution agreements, must be interpreted according to good faith. Second, it may have a 'supplementary function' which means that supplementary rights and duties, not expressly provided for in the agreement, may arise between the parties. Third, reference must be made to the very important and much debated 'restrictive' function of good faith, as set

5 See J.M.Barendrecht (1995), 'De Distributieovereenkomst' (The Distribution Agreement), in: *Dossier Advies,* No. 19, p. 85.

6 This is not because the drafting of contracts is costly. Many standard contract forms are available in Dutch Chambers of Commerce, the Dutch Council of Wholetrade in The Hague and in academic literature.

7 See J.M.Barendrecht (1995), o. c., p. 86.

8 Ibid.

9 H.E.Urlus, Personal communication, 12 August 1997.

10 J.W.A.Geel (1996), 'Inhoudsbepaling van de distributieovereenkomst' (The Definition of the Distribution Agreement), in: *Nederlands Tijdschrift voor Burgerlijk Recht (NTBR)* 1996, p. 108–109.

11 H.E.Urlus, Personal communication, 12 August 1997.

out in Article 6:248(2) of the Dutch Civil Code which means that the good faith may extinguish rules prevailing between the parties or exclude their application.[15]

This Article states that a rule binding upon the parties does not apply only to the extent that, in the given circumstances, this would be 'unacceptable' according to criteria of reasonableness and equity. However, Dutch lower courts have frequently interfered in the distribution contract and have set aside provisions that provide for a unilateral termination of the contract. In many cases the agreed notice period has been set aside and the court has forced the supplier to extend this period.

### *Provisions on the General Conditions of Contract*

If the manufacturer makes use of general conditions of contract, its termination clauses may fall under the regulation on the general conditions of contract as set out in Articles 6:231 to 6:247 of the Dutch Civil Code. Article 6:233 (a) declares voidable a clause in general conditions if it is unreasonably onerous for the other party, taking into account the nature and the other contents of the contract, the way in which these clauses have been drafted, the interests of both parties and the other circumstances of the case.

This general clause is supplemented by one list of clauses which are deemed to be unreasonable (Art. 6:236) and one list of clauses which are presumed to be so until the contrary has been proven (Art. 6:237). In principle, these are only related to consumer contracts but based on the so-called 'reflex effect' the courts can also invoke the lists in case of purely commercial transactions where one of the parties is in an unequal bargaining position.[16] This may be the case if the supplier is a large enterprise and the distributor is a natural person or a small enterprise.

This regulation may be useful to invalidate extremely unfair clauses, such as those which combine a short period of advance notice with an exclusion of any right to damages.

However, generally speaking, this regulation usually focuses on the clause itself, without reference to the circumstances under which such a clause is invoked. On many occasions, only the changed circumstances themselves will be the reason that invoking a termination clause becomes unreasonable.[17]

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12 C.A.M.van de Paverd (1999), o. c., p. 314. Van de Paverd argues that self-regulation such as a 'standard regulation' may be an option as an alternative for legislation. See p. 307–320.

13 Article 248 Book 6 reads: 1. 'A contract has not only the juridical effects agreed to by the parties, but also those which, according to the nature of the contract, result from the law, usage or the requirements of reasonableness and equity. 2. A rule binding upon the parties as a result of the contract does not apply to the extent that, in the given circumstances, this would be unacceptable to criteria of reasonableness and equity'. (Translation of P.P.C.Haanappel and E.Mackaay, New Netherlands Civil Code: Patrimonial Law (1990)).

14 Article 12 Book 3 reads: 'In determining what reasonableness and equity require, reference must be made to generally accepted principles of law, current juridical views in the Netherlands, and to the particular societal and private interests involved'. (Translation of P.P.C.Haanappel and E.Mackaay, New Netherlands Civil Code: Patrimonial Law (1990)).

*Provisions on the Commercial Agency Agreement*

In contrast to Japan, the distinction between distribution agreements and commercial agency agreements is very important in the Netherlands. This is because the agent is protected by special provisions in the Dutch Civil Code against unilateral terminations, whereas the distributor is not. For commercial agency agreements the mandatory Articles 428–445 of Book 7 of the Dutch Civil Code on specific contracts are applicable. In these provisions some minimum notice periods are set for the principal. When the principal does not abide by these periods the termination itself is valid but the agent can claim a fixed indemnity. One important provision, Article 7:442, requires goodwill compensation from the principal to the agent.

According to this Article the agent is entitled to be indemnified to the extent that he has acquired new customers or has significantly increased the volume of business with existing customers. The amount of goodwill remuneration is limited to the commission earned by the agent during one year. The sum equals the average annual commission received over the preceding five years. In some cases Dutch courts have applied these provisions by analogy to distribution agreements but usually there is no such analogous application.[18]

In Dutch actual practice many manufacturers have moved from commercial agency to distribution agreements where they want to avoid the mandatory provisions on the termination of commercial agency agreements. As a result these provisions may have lost some of their practical value. The goodwill compensation is largely seen as unjustified. The criticism is directed toward the automatic nature of such compensation, which is readily granted by the judicature without proof or other judicial examination. It does not take into consideration the specific circumstances of the case.[19] Furthermore, producers may try to prevent the application of these provisions by giving the agreement another name. In those cases the actual circumstances of the trade are determinative for defining it as a commercial agency agreement.[20]

In actual practice, it can be very difficult to distinguish between both types of contracts. It is based on a set of criteria developed in Dutch case law. For example, the distributor acts in his own name and for his own account and he is not entitled to any commission or percentage of the purchase price. Moreover, he often provides guarantees as well as after-sales customer service, and he often keeps goods in stock for his own account. Lastly, he is often in charge of his own sales promotion.[21]

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15 See on Article 6:248 for example M.W. Hesselink (1999), *De Redelijkheid en Billijkheid en het Europese Privaatrecht* (Reasonableness and Fairness and European Private Law) (PhD Thesis, Utrecht).

16 In the Explanatory Memorandum of Article 6:236 the Dutch goverament has accepted the use of this 'reflex effect', permitting the courts to invoke the lists also in the case of purely commercial transactions.

17 J.M. Barendrecht and G.R.B. van Peursem (1997), o. c., p. 175.

The most important difference with the agent is that he bears the risk with regard to the contract concluded. One further difficulty is that frequently the trade relationship can be characterised as both a distribution and agency relationship.[22] One company may act both as an agent and a distributor for various suppliers. In such cases it usually concerns non-integrated agents who perform an identical role as distributors. These agents are not really integrated in the sales network of their principal. They may also act as resellers or may represent several competing principals, thus approaching the status of a distributor.

## 3.2
## Dutch Summary Procedure

Before looking at Dutch case law it is important to refer to the Dutch system of summary procedures *(kort geding),* which has frequently been used in termination disputes. In most cases, which have ended up in court, the judgements are delivered by Presidents of Dutch District Courts in summary procedures.

Generally speaking, these procedures are used for all sorts of legal issues. The Presidents of Dutch District Courts may not issue more than a preliminary injunction in such procedures, but in practice the parties hardly ever follow up the same case with a full procedure. They rather take the preliminary injunction as a final decision in substantive law. This summary procedure before the District Courts has been used quite extensively by Dutch distributors in order to apply for an 'interlocutory' injunction at very short notice. They rarely take more than six weeks.

In most such procedures distributors have claimed specific performance of the agreement, arguing that the notice period was insufficient. Usually the underlying reason is to obtain a better bargaining position against the supplier.[23] In practice, distributors and suppliers have no desire to continue the trade relationship and both parties will negotiate as regards an adequate level of compensation to the distributor. A longer notice period will place distributors in a stronger position in such negotiations. This summary procedure frequently substitutes a full procedure. Distributors rarely turn to a full procedure before a civil court because such a procedure will take too much time.

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18 C.A.M.van de Paverd (1999), o. c., p. 37.

19 See also S.Y.Th.Meijer, *Het einde van het agentuurcontract: Een rechtsvergelijking* (The End of the Agency Contract: A Legal Comparison), in: B.Wessels, T.H.M.van Wechem (eds.) Contracteren in de Internationale Praktijk/ Deel II, p. 92.

20 District Court of Amsterdam, 19 December 1939, NJ 1941, 119.

21 See E.N.Frohn (1994), 'De Alleenverkoopovereenkomst in Nederland' (The Exclusive Distribution Agreement in the Netherlands) in: D.Kokkini-Iatridou and F.W.Grosheid (eds), *Eenvormig en Vergelijkend Privaatrecht* 1994, p. 214–216.

## 3.3
## Dutch Case Law and Legal Literature

### *Introduction*

Dutch case law is similar to Japanese case law in that it is not univocal. The Dutch court decisions on unilateral terminations of distribution contracts have been criticised due to the variety of outcomes they have produced. There is criticism of the uncertainty this produces in the law for the manufacturer-supplier and the distributor.[24] However, efforts have been made to deduce some general rules concerning the validity of such a termination, the required length of advance notice and the required level of compensation. Although the lower courts have decided most of the cases the Dutch Supreme Court has also provided some standards.

In order to draw some conclusions about the validity of a termination of a distribution agreement in the Netherlands, as in Japan, a distinction has been made between two different categories of distribution agreements: contracts of specified duration and contracts of unspecified duration. Frequently when parties first trade with one another they conclude a contract of specified duration. The supplier will first want to see whether the distributor meets its contractual obligations satisfactorily. In most cases these contracts are followed by an agreement of unspecified duration when suppliers are satisfied with the performance of the distributor.[25]

### *Distribution Agreements of Unspecified Duration*

#### – A Fundamental Right of Termination?

There has been controversy among Dutch legal scholars as regards the broader question of whether continuing contracts of unspecified duration can in principle be terminated or not. However, most contemporary scholars hold that these agreements can be terminated unless this goes against the nature of the agreement. They justify this rule on the 'complementary' function of the principle of good faith as stipulated in the Civil Code, Article 6:248.[26] The Dutch Supreme Court shares this belief.[27] Accordingly, the Dutch lower courts are also of the opinion that continuing contracts, which include distribution agreements, can be terminated, unless the nature of the agreement or the circumstances of the case dictate otherwise.

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22 See *Ubichem v. Chem-Y GmbH,* Court of Appeal of Den Bosch, 21 May 1996, NJ 1997, 280; See also *Isopad v. Huikeshoven,* HR 1 November 1991, NJ 1992, 422.

23 J.M.Barendrecht (1994), 'De redelijkheid en billijkheid en het einde van de distributieovereenkomst' (Reasonableness and Fairness and the End of Distribution Agreements), in: *NJB* 1994, p. 563, 565.

As regards the termination of distribution agreements a recent Supreme Court decision has provided an important standard. This concerned a distribution agreement of unspecified duration in which there were no contractual provisions for termination. The Court held that even if the nature of the distribution agreement dictates that it can in principle be terminated, in view of the principle of good faith, the individual circumstances of the case might dictate that the termination is only effective to the extent that there are 'serious reasons' for the termination.[28]

### *Reasons for Termination*

First, as in Japan, controversy exists in the Netherlands as regards the requirement of a good reason for the termination of a distribution agreement. In some cases the courts required a good reason.[29]

These reasons must be sufficiently serious. For example, where a distributor breaches material contractual terms and seems unwilling to rectify its performance there can be a valid reason to terminate,[30] but a statement that 'the parties did not get along with each other' or 'X did not function properly as a dealer' was not considered to be a valid reason for a correct termination.[31]

By contrast, the Dutch courts have occasionally demonstrated an entirely different approach. In Dutch case law a good reason may be an influential factor but it is not always a necessary condition per se for a valid termination. In one case the court ruled that a distribution agreements, which had lasted for 15 years, could be terminated with a reasonable notice period without disclosing the reason to the distributor.[32] In another case the court ruled that a valid termination does not always necessarily require a good reason.[33]

In Dutch legal literature a similar controversy exists but the majority of Dutch legal scholars believe that in principle a good reason is not required for a valid termination of a distribution agreement.[34] For example, a change in the supplier's marketing policies where the supplier decides to replace the distributors or to market its goods itself may already be a valid ground for termination. They are of the opinion that the protection of the distributor can be better attained by a longer notice period or a duty to compensate the distributor.

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24 See F.M.Smit (1993), 'Opzegging van Distributie-overeenkomsten' (Termination of Distribution Agreements) in: *Advocatenblad* 1993, p. 369–372; and J.M.Barendrecht (1994), o. c., p. 561.

25 According to a lawyer who is a specialist in this field, H.E.Urlus, most contracts are set for a fixed period of between one to three years after which they become contracts of unspecified duration. Personal communication, 12 August 1997.

26 See e.g. Asser-Hartkamp II (1997), *Verbintenissenrecht Deel II, Algemene leer der overeenkomsten* (The Law of Obligations Part II, General Principles of Contract), No. 310, p. 206–207; J.F.M.Strijbos (1985), o. c., p. 74; G.J.P.de Vries (1990), o. c., p. 346; J.M.Barendrecht (1994), o. c., p. 562; C.A.M. van de Paverd (1999), o. c., p. 72.

27 See for a list of decisions by the Dutch Supreme Court: Asser-Hartkamp II (1997), No. 310, p. 207– 208.

28 See *Latour v. De Bruijn,* HR 3 December 1999, RvdW 1999, 192 C.

*Termination Clauses*

Most distribution agreements in the Netherlands are concluded for an unspecified period. In most cases contractual provisions entitle both parties to terminate the agreement without any reason. In these provisions a certain period of advance notice is given. In addition, clauses are frequently included which give the right to terminate the contract immediately or at very short notice for certain (serious) reasons.[35] Examples of reasons, which entitle the manufacturer to terminate the contract immediately or at very short notice, are the non-performance of important obligations in the distribution agreement. A very important reason for cancellation stipulated in many distribution contracts is the non-achievement by the distributor of a minimum amount of annual purchases. Other reasons for termination may be insufficient marketing activities or customer service by the distributor or any other acts which might damage the interests of the manufacturer.

In Dutch law it is questionable whether immediate terminations pursuant to such provisions will be held to be enforceable. The Dutch Supreme Court has found that the enforcement of intermediate termination clauses is not permitted when the cancellation breaches the principle of good faith.[36] Although the Supreme Court emphasised that this 'restrictive' function of good faith is only applicable in special circumstances, the Dutch lower courts have often set aside these intermediate termination clauses and have extended the notice period.[37] For example, when significant investments by the distributor have not yet been recovered, a termination pursuant to the termination clause may breach good faith.[38]

Generally speaking, when contractual provisions entitle the supplier to terminate the contract these are enforceable, unless the termination violates the principle of good faith.

*Distribution Agreements of Specified Duration*

Frequently, manufacturers initially conclude contracts for a specified period in order to see whether the distributor lives up to their expectations. In contrast to Japanese case law Dutch courts hold that in principle the period agreed upon is valid and the contract cannot be terminated prior to its expiry. Any intermediate termination seems to be in contradiction to the nature of such an agreement.

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29 *Latour v. De Bruijn,* HR 3 December 1999, RvdW 1999, 192 C; *Boesjes v. PKN,* Court of Appeal of Leeuwarden, 28 November 1990, NJ 1993, 42; *Oosenburg v. Vermeulen,* District Court of The Hague, 1 September 1987, KG 1988, 293.

30 *Volvo v. Commandeur,* District Court of Haarlem, 11 December 1990, KG 1991, 34.

31 See Court of Appeal of Amsterdam, 26 January 1989, KG 1989, 118; also District Court of Utrecht, 21 June 1988, KG 1989, 117.

32 District Court of Rotterdam, 8 June 1990, KG 1991, 102.

33 *Dr. Oetker v. Expim,* District Court of Den Bosch, 30 December 1994, NJ kort 1995, 11.

34 See J.M.Barendrecht, G.R.B.Van Peursem (1997), o. c., p. 148; J.F.M. Strijbos (1985), o.c., p. 115; G.J.P.de Vries (1990), o. c., p. 350; Also C.A.M.van de Paverd (1999), o. c., p. 93.

35 J.M.Barendrecht and G.R.B.van Peursem (1997), o. c., p. 106.

The Dutch Supreme Court has found that only where unforeseen circumstances arise may a unilateral termination be permitted. However, these must be circumstances for which the party intending to terminate the agreement cannot be held liable and which are of such a nature that the other party, based on standards of reasonableness, may not expect that the agreement remains in existence as it is.[39] Article 258 of Book 6 of the Dutch Civil Code stipulates that the Courts may, at the request of one of the parties, change or completely or partially terminate an agreement based on unforeseen circumstances.

If, however, parties continue to do business after the expiry of the contractual period, the rules which apply to agreements concluded for an unspecified period are to be observed. This means that in principle such agreements can be terminated.[40]

When the parties have agreed upon an intermediate termination clause, the Dutch courts will set aside these provisions if the termination breaches the principle of good faith. The parties may sometimes even insert a clause which gives a right to intermediate termination without disclosing any reason whatsoever. However, terminations pursuant to such clauses will not readily be held to be enforceable because contracts of specified duration raise expectations with the distributor that the contract will continue until the agreed expiry date.

In contrast to Japan, the non-renewal of distribution agreements has not generated many legal disputes in the Netherlands, nor is it considered to be an important legal issue. In one rare case a supplier refused to renew the contract and insisted upon its expiry. He had repeatedly informed the distributor that he could not continue the contract in its present form. Under these circumstances the distributor, who demanded a renewal of the contract, could not rely upon the continuation of the contract.[41]

### *Compensation and Notice Requirements*

#### – Notice Requirement

In many termination disputes the essence of the dispute is the required length of the period of advance notice. Traditionally, Dutch distributors have been protected by longer notice periods.[42]

Frequently, distributors claim the specific performance of the contract and a longer notice period in order to strengthen their bargaining position. In summary procedures the

36 *Bendien v. Silten,* HR 20 april 1951, NJ 1952, 65.

37 *Volvo v. Conunandeur,* District Court of Haarlem 11 December 1990, KG 1991, 34; *Edor v. Matchbox,* Court of Appeal of Amsterdam 27 March 1986, KG 1989, 121; *Rockwool v. Maasmond,* District Court of Roermond, 2 October 1986, KG 1986, 465.

38 *Peugeot v. De Jong,* Amsterdam Court of Appeal, 26 January 1989, KG 1989, 118.

39 *Mondia v. Calanda,* HR 21 October 1988, NJ 1990, 439.

40 See J.M.Barendrecht and G.R.B.van Peursem (1997), o. c., p. 146–147; Also J.F.M.Strijbos (1985), o. c., p. 97.

President of a District Court has often forced the supplier to extend the period of advance notice and has ensured that he continues the trading relationship. In this way distributors can more easily receive compensation from the supplier because both parties will usually not want to continue the relationship.

As in Japan, what constitutes a reasonable period of notice varies with the particular circumstances of the case. It is therefore difficult to draw conclusions from case law. The courts have often held the agreed notice period to be unreasonable when the contractual relationship has continued for a long period and when there are special circumstances.[43]

An important factor is the length of the agreement. The longer the agreement the longer the period of notice. Another factor is the degree to which the distributor is dependent on the supplies of the supplier. In one case where the distributor was 40 percent dependent on the productline from the supplier, the court changed a three-month notice period into a one-year period. The distribution relationship had lasted for 30 years.[44] Finally, one important factor does constitute the reason for the termination. When serious reasons for termination exist, such as fraud by the dealer[45] or an unwillingness to discuss improvements to the turnover,[46] the supplier can terminate without even providing any notice.

Dutch courts and legal scholars have argued that in general a period of six months would be a reasonable notice period. This would also be the maximum period because in this way both parties would not unwillingly have to continue their relationship for an extended period.[47] The same motivation has prompted the Dutch legislator to set the maximum notice period for the termination of agency agreements at six months.

– Compensation

Termination disputes in which the distributor claims compensation are rare in the Netherlands. This is because proceedings concerning the length of an advance notice are aimed at restricting the supplier and creating as much room for negotiation as possible.[48]

However, a new development in Dutch case law is that even if the advance notice period is considered to be reasonable, the supplier may be required to compensate the distributor in the form of damages. The Dutch Supreme Court has held that these damages are due when investments made by the distributor in reliance on the continuation of the contract are not compensated by an otherwise reasonable notice period. Despite the fact that the supplier had given a reasonable notice period of three months, the Supreme Court ordered the supplier to compensate the distributor. The latter had made significant investments such as advertising costs, building costs and extra costs incurred for laying off redundant personnel. These investments had not been recovered at the time when the notice period

41 *Ixtribute v. Informix Software,* District Court of Utrecht, 20 May 1997, KG 1997, 219.

42 J.M.Barendrecht and G.B.R.van Peursem (1997), o. c., p. 152.

43 See *Volvo v. Commandeur,* District Court of Haarlem, 11 December 1990, KG 1991, 34: *Peugeot v. De Jong,* Court of Appeal of Amsterdam, 26 January 1989, KG 1989, 118; *Edor v. Matchbox,* Court of Appeal of Amsterdam 27 March 1986, KG 1989,121.

44 See *Edor v. Matchbox,* Court of Appeal of Amsterdam 27 March 1986, KG 1989,121.

had expired.[49] This compensation was justified by the 'complementary' function of the principle of good faith.

This decision has given rise to a discussion about the degree to which the distributor may be protected. Many legal scholars support this decision. They argue that there may be many cases in which the notice period may not be sufficient to compensate for the investment made by the distributor. However, critics have argued that distributors are independent merchants who invest at their own risk. Only when the 'behaviour' of the supplier has induced the distributor to make the investments, will this kind of duty to pay damages arise.[50]

In several other cases the Dutch lower courts have also found that the distributor should be compensated for investments which could not be recovered.[51] According to case law an obligation to compensate may also replace an adequate notice period. For example, it may replace the required period to make the necessary adaptations for a new distribution relationship.[52]

There is, however, no clarity in Dutch law about the method for calculating these damages. Generally speaking, compensation is required for investments which have been made in order to meet contractual obligations. Examples may be advertisement costs, the costs of constructing showrooms or selling space, facilities for repair or laying off redundant personnel.

Controversy exists as regards compensation for the loss of clients, the so-called 'goodwill compensation'. Unlike the case of commercial agency agreements there is no statutory rule entitling a distributor to goodwill compensation. When the rules for the protection of the commercial agent were enacted in the Dutch Civil Code the Minister of Justice rejected any interpretation by analogy to distributors.[53] In case law this analogous interpretation is very rare. Only in one case did the court decide that the distributor should be entitled to goodwill compensation. The court justified this decision on the principle of good faith.[54]

Most Dutch legal scholars argue that there are no grounds for such analogous interpretation. They contend that although distributors may sometimes find themselves in a similar position as the agent, they cannot claim goodwill compensation because they tend to be much more independent than commercial agents and will have mostly built up

45 *Pon-Porsche v. K.,* District Court of Breda, 25 May 1988, KG 1988, 248.

46 *Jamca v. Berger du Nord,* District Court of Zwolle, June 13, 1986, KG 1986, 311.

47 *Dr. Oetker v. Expim,* District Court of Den Bosch, 30 December 1994, NJ kort 1995, 11; *VDK v. Mori Seiki,* District Court of Rotterdam, 8 June 1990, KG 1991, 102.; See J.M.Barendrecht, G.B.R.van Peursem (1997), o. c., p. 152; C.A.M.van de Paverd (1999), o. c., p. 107–110.

48 H.E.Urlus, Personal communication, 12 August 1997.

49 *Mattel v. Borka,* HR 21 July 1991, NJ 1991, 742.

50 See the note by P.A.Stein in *Mattel v. Borka,* HR 21 July 1991, NJ 1991, 742. On this issue he refers to the PhD thesis by J.F.M.Strijbos (1985), o. c., p. 164. The same argument was expressed by the District Court of Leeuwarden. See *VDM v. Vastgoed,* District Court of Leeuwarden, 27 July 1994, No. 180/94. (not reported).

goodwill by themselves. Furthermore, the distributor will in most cases continue to make use of the customer base which he has established.[55]

## 3.4 Conclusion

It can be concluded that the validity of a termination of a distribution agreement varies from case to case. It is evident that the courts have often set aside the contractual provisions concluded between the parties. This limitation on the freedom of contract by judicial interference is based on the premise that, given the way both parties commence the contractual relationship, they are not in a position to decide by themselves how the contracts can be terminated. One of the reasons is that usually there is a great difference in bargaining power between the supplier and the distributor. Furthermore, unilateral terminations usually occur after many years when circumstances may have considerably changed.[56] For example, the contractual relationship may have continued for longer than was expected by the parties, which may render any short notice periods to be no longer adequate. Furthermore, in case the distributor has made significant investments, which have not been recovered at the time the contract is cancelled, compensating the distributor may be necessary.

Although the Dutch courts have at times protected the distributor, in actual practice Dutch distributors are hardly protected at all by Dutch contract law. Summary procedures are easily accessible to them, but the parameters are too vague, which prevents many distributors from bringing an action for a longer notice period and the specific performance of the contract.[57] Claims for damages are rare, since these can usually only be made in full procedures which take a long time. Furthermore, distributors must present sufficient evidence to prove the existence of a long-term trading relationship, the damages incurred because of the termination and the fact that investments have not been recovered at the time the agreement is terminated. This can be very difficult in practice.

The influence of applicable Dutch contract law on the drafting of contracts or the terminating behaviour of suppliers seems to be rather limited. Contract stipulations often exclude any ancillary obligation to compensate for any resulting loss upon termination. This means that the preventative drafting of distribution agreements is not very common.[58] Furthermore, Dutch suppliers often terminate as soon as possible once they find a better

51 *Van den Eynden v. Over Look Textil,* District Court of The Hague, 30 October 1996, KG 1996, 359; *Tendem v. Ebas,* District Court of Haarlem, 9 August 1995, PRG 1996,4491.

52 See *Dr. Oetker v. Expim,* District Court of Den Bosch, 30 December 1994, NJ kort 1995, 11.

53 In the draft for the new Bill on agency agreements this analogous interpretation was rejected. See MvA II, Kamerstukken 20842, No.6.

54 *Siero v.Contilack,* Court of Appeal of Amsterdam, 3 October, 1996, No. 946/95. (not reported).

55 F.M.Smit (1993), o. c., p. 370.; See also C.A.M.van de Paverd (1999), o. c., p. 181; J.M.Barendrecht and G.B.R.van Peursem (1997), o. c., p. 164.

business partner. Usually the necessary cost efficiency attained by giving a short period of notice is seen as more important than the reasonableness of the notice period or any required compensation.[59]

*Comparison with Japanese Law*

Dutch case law shares certain similarities with Japanese case law. Judicial intervention arising from the unilateral termination of distributorship agreements in both Dutch and Japanese law has been problematic. As in Japan most decisions have come from lower courts and they have displayed a wide variety of approach. In both countries there are no clear parameters in relation to notice requirements and compensation. Furthermore, in both countries a controversy exists as regards the requirement of a good reason for a valid termination of the distribution agreement.

It seems, however, that distributors receive slightly more protection under Japanese case law, which is reflected in the Japanese method of judicial reasoning. The Japanese courts have usually gone further in requiring a good reason for the termination. The concepts used by Japanese courts such as the 'breakdown of the relationship of trust' or 'unavoidable reasons' for a valid termination seem to indicate this.

Another similarity between Dutch and Japanese case law can be discovered in the expansive use of good faith by the courts to interfere in the distribution contract and set aside provisions which provide for a unilateral termination of the contract.[60] In many cases the agreed notice period has been set aside and the court has forced the supplier to extend this period.

However, compared to the Japanese courts, Dutch courts pay slightly more attention to the contents of the underlying formal contractual terms. This may, for example, be illustrated by the fact that they have ruled that agreements, which are concluded for a fixed period, cannot in principle be terminated prior to the expiry of the contract. By contrast, in Japanese case law in most cases the courts make almost no distinction between contracts concluded for a fixed period and those concluded for an indeterminate period.

Generally speaking, Dutch judges less readily modify the meaning of clearly and agreed-upon term at their own discretion. As is common in most legal systems, Dutch courts rather intervene by invalidating terms if they believe that these terms violate the principle of good faith. In Dutch law this is based on the 'restrictive' function of good faith.

Another difference is that in contrast to Japanese law, in Dutch law commercial agents are more protected than distributors. The provisions on commercial agents in the Dutch

56 See J.M.Barendrecht (1994), o. c., p. 564.

57 H.E.Urlus, Personal communication, 12 August 1997.

58 Ibid.

59 Ibid.

Civil Code have sometimes even been applied by analogy to distribution agreements. Accordingly, the Dutch courts more readily distinguish the differences among the various types of contracts within the Dutch distribution sector. They draw a more clearly defined distinction between the termination of a distribution agreement and a commercial agency agreement.

Generally speaking, it may be questioned whether in actual practice there is much difference in the degree to which Dutch and Japanese distributors are protected by contract law in the case of unilateral terminations of distribution agreements by manufacturers. In both countries judicial intervention on the basis of good faith has provided little certainty in the law, which still tends to function as a barrier to litigation. However, one important difference may be that the Japanese equivalent of the Dutch injunction proceedings *(karishobun)* does not function as well as in the Netherlands. In contrast to Japan, Dutch distributors have a strong weapon by which to increase their bargaining power in the form of summary procedures.

## 4
## ANTI-TRUST LAW

### 4.1
### Introduction

The EU anti-trust rules, as set out in the Treaty of Rome, are designed to preserve effective competition and to facilitate the operation of a single market. The aim is to prevent barriers being erected by private agreements between businesses or the abuse of monopolies. Furthermore, the anti-trust rules encourage efficiency, innovation and lower prices. In addition, the national anti-trust laws of the Member States are designed to preserve effective competition within their countries. As in Japan, where the Anti-monopoly Act has a similar function, these rules can have an important indirect influence. They can also set limits on the principle of freedom of contract and the possibilities of terminating a distribution agreement at will.

First, EU and national competition law can be enforced by the national civil courts, and in some cases distributors can assert that the termination itself, or the clauses 'justifying' it, violate anti-trust rules. As in Japan, this can also be combined with a complaint, or a threat to do so, with a competition authority (the EU Commission or the Dutch Competition Authority).

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60 For example in French law it is the doctrine of abuse of rights which is adopted by the courts to set aside termination clauses. However, French courts are more reluctant than Dutch courts to set aside these clauses. In German law the good faith doctrine has a similar function as in the Netherlands but the termination clauses are more closely examined under the provisions on general conditions of contract (AGB-Gesetz). See J.M.Barendrecht and G.B.R.van Peursem (1997), o. c., p. 172–173.

Second, substantive EU and national anti-trust law influence the drafting of distribution agreements and the way in which distribution channels are formed. They can have an impact on the way termination clauses are drafted by the manufacturer. This particularly applies to termination clauses in agreements concluded within the automobile industry and in selective distribution systems.

Therefore, when comparing Japanese anti-trust law as it applies to agreements within the distribution sector with anti-trust law in the Netherlands, it is important to realise that in the Netherlands not one but two types of rules may be applicable. EU Anti-trust rules may apply if and to the extent that agreements, decisions and practices influence trade between Member States. National anti-trust law may apply when competition is only impeded within the Netherlands. With the new Dutch Competition Act Dutch anti-trust law now almost completely mirrors EU law.

First, I will briefly refer to EU and Dutch substantive anti-trust law as compared to the applicable Japanese law. This also requires a brief reference to the organisation and procedure. My main focus, however, centres on the private law influence of a violation of anti-trust law and the relationship between the civil courts and the competition authorities.

## 4.2 EU Anti-trust Law

### *Substantive EU Anti-trust Law*

As far as commercial agreements such as distribution agreements are concerned, the key provision in EU substantive anti-trust law is Article 81(1)[61] of the EU Treaty, which prohibits agreements that affect trade between Member States and restrict competition within the market.[62] Article 81(2) renders these agreements unenforceable in whole or in part. In order to determine that an agreement is in violation of Article 81(1) the Commission must establish that a restriction of competition exists, that the restriction is appreciable and that it affects trade between the Member States.

However, this ban on restrictive agreements has been somewhat softened by the exemption rule of Article 81(3), which allows the Commission to exempt agreements if it concludes that the competitive aspects of the agreement outweigh the harmful effects which the agreement has on competition.

#### – Restrictions in Vertical Arrangements

Generally speaking, EU substantive law as it applies to restrictions within the distribution sector is not so very different from the equivalent Japanese anti-trust law.[63] As in Japan, in the context of a vertical arrangement one of the most serious transgressions is resale price maintenance, where the supplier effectively imposes a resale price on its distributors.[64]

However, one important difference is that there is much more clarity in EU anti-trust law concerning which vertical restrictions constitute a violation. For example, in relation to non-price vertical restraints there is a greater number of formal decisions by the

Community Courts and the European Commission than by the FTC or the Tokyo High Court in Japan. Furthermore, there are so-called EU block exemptions which provide more information than in Japan about which restraints constitute a violation of anti-trust law.

– Block Exemptions

According to Article 81(3), in order to secure an exemption from Article 81(1) an agreement must either be the subject of a notification to the Commission or it must satisfy the conditions set out in the block exemptions. In order to reduce the costs of a notification of each agreement the Commission had adopted a series of block exemptions. As far as vertical agreements are concerned, there are currently four block exemptions: the block exemption for exclusive distribution contracts,[65] exclusive purchase contracts,[66] franchise contracts[67] and motor vehicle distribution contracts.

The Motor Vehicle Block Exemption of 1995 directly protects the distributor against unilateral terminations of the distribution agreement.[68] In this Block Exemption the Commission has imposed some minimum notice periods upon the supplier when it intends to terminate the agreement with the dealer. The Commission wanted to prevent a strong dependence on the part of the dealer upon the supplier due to short-term agreements or short notice periods for termination.[69]

In Dutch practice these exemptions have a great deal of influence since many manufacturers have decided to reproduce the model distribution contracts in the block exemption, in order to ensure that they do not violate EU law.[70]

It is important to note that on July 1, 2000, except for the Motor Vehicle Block Exemption, these exemptions will be changed into one single umbrella Block Exemption Regulation with market thresholds and a 'black list' approach to asses agreements. This list includes restrictions which are considered to be inherently restrictive of competition. This

61 Article 81(1) reads: "The following shall be incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between member states and which have as their object or effect the prevention, restriction or distortion of competition within the common market". (Until May 1999 this Article used to be Article 85(l)).

62 In addition, Article 82, which prohibits any abuse of a dominant position, can at times also be important for distributors. This Article prohibits any abuse of a dominant position by one or more firms in a substantial part of the Common Market that may affect trade between the Member States. A supplier with a dominant position in the market may, under certain circumstances, abuse this position if he withdraws supplies suddenly or without notice. See Lennart Ritter, W.David Braun and Francis Rawlinson (1993), *EEC Competition Law,* p. 302.

63 See Hiroshi Iyori (1997), *Dokusen kinshi seisaku to dokusen kinshihō* (Anti-monopoly Policy and the Anti-monopoly Act), p. 633,657. I will not provide a detailed analysis of the differences since that falls beyond the scope of my thesis.

64 However, according to H.Iyori, compared to EU anti-trust law the Japanese regulation of resale price maintenance is more rigid. Furthermore, in Japan there are more cases of violations of the resale price maintenance prohibition. See H.Iyori (1997), Ibid., p. 630–631.

means that agreements are only examined according to what cannot be exempted instead of what can be exempted.[71]

– EU Anti-trust Law on Selective Distribution Agreements

In addition, it is important to describe the law as it applies to selective distribution agreements[72] which form an important category within the EU and which are used, for example, in the distribution system for luxury cosmetics. In the absence of a block exemption the Commission's practice is reflected in nearly 20 formal decisions taken over the course of a number of years, statements published in the Commission's annual competition reports, and judgements by the Community Courts.

This policy which governs the establishment and operation of these selective distribution agreements includes the fact that selective distribution networks fall outside the Article 81 (1) prohibition if three conditions are met: the nature of the goods is such that selective distribution is necessary if they are to be properly distributed; distributors are selected solely on the basis of qualitative criteria, which are not excessive but ensure that the goods are distributed under appropriate conditions; and the qualitative criteria for admission to the network are applied objectively and without discrimination.[73]

Accordingly, the Commission has not only been active in relation to the selection of retailers but also in relation to the termination of selective distribution agreements. Although there are no specific rules concerning the term and the termination of selective

65 Commission Regulation 1983/83 [1983] O. J. L 173/1.

66 Commission Regulation 1984/83 [1983] O. J. L 173/5. However, these first two regulations indirectly damage the interests of distributors. This is because they prohibit the use of post-contractual non-competition clauses. Suppliers who have concluded exclusive distribution or exclusive purchasing agreements with their distributor and intend to terminate the agreement will more readily terminate at very short notice. This is because they want to prevent any competition from the distributor, which may start directly after the latter has realised that the supplier intends to terminate the contractual relationship.H. E. Urlus, Personal communication, 12 August 1997.

67 Commission Regulation 4087/88 [1988] O. J. L 359/46.

68 Commission Regulation 1475/95 of June 28, 1995 on the application of Art. 81(3) on the EU Treaty to certain categories of motor vehicle distribution agreements [1995]. O. J. L 145. This Regulation will be excluded from the forthcoming reforms.

69 Article 5 stipulates that if parties choose to conclude an agreement of specified duration there must be a minimum initial contract period of 5 years. Furthermore, each party must disclose at least 6 months before the expiry of the period if it does not intend to renew the contract. When the parties have concluded an agreement of an indeterminate period, there must be a minimum advance notice of 2 years. The latter period can be reduced to one year if the supplier provides adequate compensation. However, these obligations do not apply when the supplier needs to reform the distribution system and provides a minimum of one year's notice or when one of the parties breaches an essential obligation in the agreement.

70 According to M.B.W.Biesheuvel, who is very critical of these Block Exemptions, more than 50 percent of all Dutch distribution agreements are exact copies of the models provided by the Block Exemptions. Personal statement during a symposium on Distribution Agreements at the University of Brabant (KUB), Schoordijk Instituut on 11 March 1998.

distribution agreements, the selection of dealers may be closely related to their expulsion from the network.[74] The Commission and the Community Courts have established that a termination of an agreement because of failure to comply with criteria other than qualitative criteria infringes Article 81(1) of the EU Treaty.[75]

For this reason the provisions for termination always receive considerable attention from the Commission.[76] The Commission wants to prevent termination or the threat of termination of the agreernent being used to enforce disguised restriction on competition such as resale price maintenance. This applies, for example, to cases where termination by notice can be given without disclosing any particular reason for such termination.

For example, in one case the Commission demanded that a manufacturer should amend the termination clauses which enabled it to terminate the agreement because of a failure to comply with criteria other than the general objective criteria. Under the new agreement such termination was only valid in the event of a complete change of the distribution system involving the termination of all distribution agreements. The new agreements entitled the manufacturer to terminate without notice but reasons always had to be given.[77]

Finally, it is important to note that the selective distribution agreements will also fall under the single umbrella Block Exemption Regulation which will enter into force on July 1, 2000.

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71 One of the EU Commission's objectives for this change is to provide companies with greater legal certainty by removing the straitjacket of the existing block exemptions. See J.Nazerali and D. Cowan (1999), 'Reforming EU Distribution Rules—Has the Commission Found Vertical Reality?', in: *E.C.L.R.* 1999, p. 159–168.

72 In a selective distribution network the supplier undertakes to supply its products only to dealers and retailers who satisfy certain professional or technical requirements, employing suitably trained staff and operating from premises deemed appropriate for its products. Members of the network agree to refrain from selling to businesses outside the authorized network. These systems are typically used for the sale of sophisticated consumer items such as luxury cosmetic products.

73 Recently confirmed in the Givenchy and Yves St Laurent Perfums decisions. See *Yves Saint Laurent Parfums, 16 December 1991*, O. J. 1992 L 12/24.; Parfums Givenchy, 24 July 1992, O. J. 1992 L 236/11.

74 Because of a wide interpretation of 'agreements' by the Court of Justice a unilateral act such as a refusal to trade may also violate Article 81. Accordingly, this means that a selective distribution system in which the contractual agreements adopted are in accordance with EU law, may still violate anti-trust law in the way the system is actually operated. See Case 107/82 *AEG-Telefunken v. Commission,* 25 October 1983, [1983] ECR 3151; Case 25–26/84 *Fordwerke and Ford Europe v. Commission,* 17 *September* 1985, [1985] ECR 2725; Case C–70/93, BMW/ALD Autoleasing, 24 October 1995, [1995] ECR I 3439.

75 This approach is reflected in a number of formal decisions by the Commission and judgments by the Community Courts. See e.g. Case 26/76, *Metro v. Commission,* 25 October 1977, [1977] ECR 1875; Case l07/82 *AEG-Telefunken v. Commission,* 25 October 1983, [1983] ECR 3151.

*Public Law Enforcement of EU Anti-trust Law*

According to some well-known Japanese legal scholars the differences of EU anti-trust law with Japanese anti-trust law are not much found within substantive law, but rather in the rigidity of enforcement by the competition authorities. Compared to Japanese anti-trust law the enforcement of anti-trust law by the EU Commission and the Community Courts has been stronger and more formal.[78] The enforcement of EU anti-trust law is primarily entrusted to the EU Commission. It is entrusted to a staff of 200 officials in the Commission's Competition Service, DG IV.

An important difference with Japan, of course, is that in the EU not only the Commission but also the national competition authorities in each Member State may enforce EU anti-trust law.

Another important difference with Japan is found in the notification system. The start of an investigation by the Commission may not only follow from a complaint or an *ex officio* initiative but also from an application for negative clearance[79] of a notification for an individual exemption.[80] This notification system has triggered many notifications which provide the Commission with much information about transactions, including vertical agreements. In actual practice a substantial portion of the Commission's decisions are triggered by these notifications.

However, the Commission mainly works in an informal way. In most cases the Commission grants negative clearance from Article 81(1) by informal settlement in so-called 'comfort letters'.[81]

Although they do not provide comprehensive legal certainty, these comfort letters carry considerable authority, because they indicate the Commission's assessment of the agreement. Although not legally bound by a comfort letter, no national authority or national court has ever issued a decision which is at odds with the position expressed in such a letter.[82]

In the event that the Commission concludes that the activities constitute a violation of Article 81(1) following an investigation,[83] it issues a statement of objections which consists of a letter addressed to the enterprises engaged in the activities in question. In this letter the Commission must clearly set out the essential facts on which the objection is based. After the concerned enterprises and interested third parties have been given the opportunity

76 R.Christou (1996), *International Agency Distribution and Licensing Agreements,* p. 251. See Case 86/82 *Hasselblad v. Commission,* 21 February 1984, [1984] ECR 883.

77 See Case 75/84, *Metro v. Commission* (No.2), 22 October 1986, [1986] ECR 3021.

78 H.Iyori (1997), o. c., p. 613–614, 657; Masahiro Murakami (1997), *Dokusen kinshihō kenkyū* (An Investigation into the Anti-monopoly Act), p. 83–85.

79 This means an application for a formal certification by the Commission that the transaction described in the application does not constitute a violation of Article 81(1).

80 This means the notification of an agreement which is prohibited by Article 81(1) but for which the party seeks an exemption pursuant to Article 81(3).

to reply or make known their views the Commission may issue its final decision. Appeals can be filed with the Court of First Instance and subsequently to the Court of Justice.

## 4.3
## Dutch Anti-trust law

### *Substantive Dutch Anti-trust Law*

When competition is only affected or restricted within the Netherlands and does not affect trade between the Member States, Dutch national anti-trust law is applicable. With the new Dutch Competition Act which was enacted on January 1, 1998,[84] Dutch domestic anti-trust law has almost completely followed the approach taken in EU anti-trust law. The Act is partly due to increasing outside pressure from the OECD and the Commission which criticised the Dutch consensus economy, where many decisions are reached by consensus, including those on prices and other trading conditions.[85]

The new Act has a considerable impact on the day-to-day activities of companies in the Netherlands. So far, it can be concluded that the Act amounts to nothing short of a revolution in anti-trust policy in the Netherlands. Under the old system restrictive agreements were only forbidden if the Minister of Economic Affairs had taken an explicit decision to this effect. The Dutch distribution sector had very much profited from this system which had existed for 40 years. Therefore most criticism against the Act has been voiced by this sector.

The new Act largely mirrors EU anti-trust law.[86] For example, Article 6 of the new Act contains a general prohibition on restrictive agreements, decisions and practices modelled according to the provisions of Article 81 of the EU Treaty. This article also stipulates that agreements which restrict competition are void per se.[87] The Act has also introduced in Article 24 the concept of a prohibition on abusing a dominant position, derived from Article 82 of the EU Treaty.

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81 It is estimated that 95 percent of all notifications to the Commission are dealt with informally by way of comfort letters. See M.B.W. Biesheuvel, M.R. Mok and H.G. Sevenster (1996), 'Van ordening naar marktwerking: kanttekeningen bij het ontwerp Mededingingswet': Preadvies voor de Vereniging 'Handelsrecht' en de Vereniging voor Mededingingsrecht, p. 44 note 96.

82 This informal approach of granting comfort letters may be comparable to some extent to the prior consultation system provided by the Guidelines of 1991 in Japan.

83 The Commission's power to investigate include, for example, information requests, on-site inspections, and obtaining assistance from Member States in conducting investigations.

84 The new Act replaced the old Dutch Economic Competition Act *(Wet Economische Mededinging)* which was based on the notion of abuse. Under this Act anti-competitive agreements were allowed unless the Ministry of Economic Affairs had declared them to be inoperative on the ground that they were detrimental to the public interest.

85 See Pierre Bos (1996), 'Het voorstel voor een nieuwe Mededingingswet: de sprong van us mem naar het paard van Troje' (The Proposal for a New Competition Act The Jump from us mem to the Trojan Horse), in: *NJB* 1996, p. 1237.

The Act provides for many exemptions with respect to the prohibition of Article 6 roughly along the same lines as EU anti-trust law. For example, the Dutch Competition Authority will not take action against agreements which are considered to be of minor importance.[88] This exemption is very important for the distribution sector. In addition, the prohibition does not apply to agreements to which the Commission has granted an individual or group exemption concerning the pro-hibition of Article 81 of the EU Treaty.

Finally, some reference must be made to the 'national' group exemptions. The Minister of Economic Affairs had partly yielded to pressure from the distribution sector and by general administrative order he had declared some vertical restrictions to be exempt.[89]

### *Public Law Enforcement by means of the Dutch Competition Authority*

The new Act has also created an entirely new Dutch Competition Authority with currently a staff of approximately 120 persons, which is entrusted with the enforcement of the new rules.[90] In the first year of its existence it officially had to report to the Ministry of Economic Affairs but on January 1, 1999, it became a totally independent administrative body. It is headed by a Director General and consists of one staff section and three operational sections under responsibility of the Director General.

The enforcement procedures of the Dutch Competition Authority are patterned after the EU Commission's procedures for enforcing EU anti-trust law. The enforcement procedure is laid down in the Act. The General Act on Administrative Law *(Algemene Wet Bestuursrecht),*[91] as a general procedural act, applies furthermore to the enforcement procedure.

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86 In the Explanatory Memorandum to this Act it is explicitly stated that by adopting the wording of Articles 81 and 82 as far as possible, the aim is to ensure that the application of the Act shall be significantly influenced by the decisions of the Commission and the judgements of the Community Courts. See Explanatory Memorandum p. 10.

87 Article 6 reads: 1) 'Agreements between undertakings, decisions by associations of undertakings and concerted practices by undertakings which have as their object or effect the prevention, restriction or distortion of competition within the Dutch market, or a part thereof, are prohibited. Agreements and decisions prohibited pursuant to Clause 1 are legally null and void'. (Translation by the Dutch Competition Authority. To be found in its homepage on: http//www.nma-org.nl.).

88 In Article 7 it is stipulated that there is an exemption with respect to agreements between no more than eight companies with a collective turnover, in the case of companies involved in the sale of goods, of no more than 10 million guilders. This is at variance with the thresholds found in EU law.

89 See Article 15 of the Act; See also J.C.M.van der Beek (1998), Gevolgen van de nieuwe Mededingingswet voor de distributie sector (The Consequences of the new Competition Act for the Distribution Sector), in: *Advocatenblad* 1998, p. 81–86. This exemption does not include exemptions for resale price maintenance. The only remaining exemption for resale price maintenance is for Dutch books and journals.

90 See also on the enforcement by the Dutch Competition Authority, including its decisions, its homepage on: http//www.nma-org.nl.

In order to enforce national anti-trust law it has powers to carry out investigations and grant or refuse an exemption from the prohibition of Article 6. Furthermore, it has powers to impose fines and orders sanctioned by periodic penalty payments to those violating the anti-trust rules. The Dutch Competition Authority may also apply EU anti-trust rules pursuant to Article 88 of the EU Treaty.

The commencing of an investigation by the Dutch Competition Authority may follow from a complaint, an *ex officio* initiative and a notification for an exemption. If based on the information acquired during the investigation, a reasonable presumption of a violation exists for which a fine or a penalty should be imposed, the investigating officials must draw up a report (similar to the 'Statement of Objections' of the Commission), which institutes the second phase of the enforcement procedure. Before reaching a final decision, interested parties, including third parties, having the required interest, are given the opportunity to present their views either orally or in writing.

Compared to EU law, however, Dutch rules on procedure are generally more strict. For example, a decision on an agreement, which is notified in order to obtain an individual exemption, must be made within fixed time limits (four months, which term may be extended once by a further four months).[92]

Since the enactment of the new Act many standard-form distribution agreements have been notified in order to obtain an individual exemption.[93] In actual practice many contracts have also been shown for prior approval by asking for an informal 'provisional view' *(voorlopige zienswijze)* from the Dutch Competition Authority. By means of consultation with manufacturers standard-form contracts have often been adjusted. In relation to termination clauses the Dutch Competition Authority has looked at the ease with which manufacturers are entitled to terminate their contracts.

Legal protection against the decisions of the Director General of the Dutch Competition Authority is twofold. First, the parties can file an administrative appeal *(bezwaar)* with the Authority. This appeal is free of charge and so far it has been lodged frequently. Second, after this first appeal a second appeal can be lodged at the District Court of Rotterdam (Chamber for Administrative Law). Finally, the Court of Appeal for Trade and Industry is competent to hear an appeal in the second and final instance. The latter two appeals may turn out to be expensive because the parties must be represented by a lawyer. So far these appeals have rarely taken place.

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91 Algemene Wet Bestuursrecht. Act of 4 June 1992, Official Journal 1992, 315.

92 Article 19 of the Dutch Competition Act.

93 For example, in one case four importers of foreign books had notified their terms of delivery very in which individual resale price maintenance was included. On 16 December 1998 the Dutch Competition Authority decided that no exemption could be granted. Dutch Competition Authority Decision, *BV van Ditmar Boekenimport,* 16 December 1998, No. 450.

## 4.4
## Private Law Enforcement of EU and Dutch Anti-trust law

### *EU Anti-trust Law*

As in Japan increasing importance is being attached to the interrelationship between private law and anti-trust law and the use of private law to enforce anti-trust law. In addition to a claim for specific performance or damages distributors can also invoke Article 81(1) before the national Dutch civil courts, since it has direct effect in all Member States. Article 81(2) declares agreements and practices contrary to Article 81(1) to be automatically void but its implementation is left to the domestic law of each Member State.

In the Netherlands distributors can invoke Article 81(2) in conjunction with Article 3: 41 of the Dutch Civil Code, which provides for partial nullity.[94] Accordingly, if the clause on which the supplier justifies the termination infringes Article 81(1), the distributor may invoke its nullity. For example, when manufacturers stop supplying to distributors because they do not sell at the resale price indicated in a contractual provision, this clause may be declared null and void. This may render the termination without valid reason and may thus be unenforceable. Finally, an infringement of Article 81(1) may sometimes also be considered a violation of the law and therefore a wrongful act, as stipulated in Article 6: 162 of the Dutch Civil Code.[95]

However, Dutch distributors face difficulties which are comparable to the difficulties faced by distributors in Japan. First, suppliers will usually not use contract provisions which are in clear violation of Article 81(1) of the EU Treaty. Furthermore, in the absence of such clauses they will usually not justify the unilateral termination with the non-compliance of a forbidden trade practice by the distributor.

Furthermore, as in many other Member States[96] the enforcement of EU anti-trust law by the Dutch civil courts is still relatively under-developed. Generally speaking, a gap exists between EU anti-trust law as it is applied by the Community Courts and the Commission and EU anti-trust law as it is applied by the Dutch civil courts, which is somewhat disadvantageous for plaintiffs. The Dutch courts are reluctant to apply Articles 81 and 82, certainly when the consequences may be important. If these Articles are applied they are often interpreted and applied in such a way that the status quo of an agreement as far as

94 Article 3:41 reads: "The nullity of part of a juridical act does not affect the rest of the act, to the extent that, taking into consideration the content and necessary implication of the act, the parts are so inextricably related so as not to be severable". There is, however, very little literature and case law on this issue. See M.B.W.Biesheuvel, M.R.Mok and H.G.Sevenster (1996), o. c., p. 25.

95 In one case a distributor successfully petitioned the District Court for an injunction in a summary procedure to deliver the products. He based his claim on Article 86 (currently Article 82) of the EU Treaty and Article 1401 BW (Old Dutch Civil Code). The court found in favour of the distributor, declaring that the supplier had abused its dominant position. See, *Van Gelderen Import BV v. Impressum Nederland BV,* District Court of Amsterdam, 5 April 1979, NJ 1981, 129.

96 See Lennart Ritter, W.David Braun and Francis Rawlinson (1993), *EEC Competition Law,* p. 708.

possible remains unaffected.[97] Two reasons are given for this gap. First, it is important to realise that a large majority of decisions are delivered in summary procedures. The Presidents of the District Courts in these procedures often assert that the circumstances are too complex to justify a decision in which a provisional measure is given.[98] Furthermore, particularly in such an expeditious procedure where judgements are usually granted within two or three weeks of the oral pleadings it will be all the more difficult for litigants such as distributors to gather sufficient evidence to prove that EU anti-trust law has been violated.[99]

A second explanation for this gap may be the lack of any anti-trust concepts in the Dutch national legal system.[100] Predecessors to the new Act did not provide for very clear prohibitions on anti-competitive agreements and they were rarely enforced before the Dutch civil courts. Furthermore, many decisions within the Dutch economy are reached by consensus. Finally, anti-trust law is not one of the compulsory subjects in most law faculties.[101]

So far, instead of justifying the invalidity of a termination of a distribution agreement on a violation of EU anti-trust law Dutch civil courts usually justify such decisions on the good faith doctrine.[102] Only in a few number of cases did the courts apply EU anti-trust law in order to invalidate the termination.

In one case a dealer had concluded an exclusive distribution agreement for an indeterminate period with an importer of farm machinery. This dealer received the exclusive dealership for one part of the Netherlands to sell a famous brand of tractors. Approximately 20 years into the agreement the importer agreed with the Dutch organisation of dealers which were selling this brand that its dealers should not import and resell any tractors which were younger than one year. This agreement was notified orally to all dealers. After the importer discovered that the dealer had repeatedly imported and resold new tractors, he terminated the agreement with seven months' notice. In response, the dealer

97 See I.W.Verloren van Themaat, N.W.Adema, F.Rijnsbergen, J.F.Schutte and K.Sevinga, Dutch Report prepared for the XVIIIth FIDE Conference in Stockholm in 1998, p. 212; Also in: 'National Application of Community Competition Law', in: *Sociaal-economische Wetgeving (SEW)* 4 1998, p. 137-148.

98 For example, in cases where Article 82 is invoked it is difficult to assess whether the firm has a dominant power position within the Common Market. The President may rule that the parties must start a full procedure before the civil court. See e.g. a recent termination dispute within the publishing industry: *Edipress International v. Betapress Van Gelderen Import,* 4 March 1997, No. 34126/KG ZA 97–82 (not reported).

99 Even if a full procedure would be initiated procedural means such as the hearing of parties in person or the hearing of witnesses will in most cases not be enough to obtain sufficient evidence.

100 Dutch FIDE Report of 1998, p. 213.

101 Ibid.

102 See e.g. *Helena Rubinstein v. Devecos,* District Court of Haarlem, 24 July 1992, No. 1597/1992 (not reported) and *Etos v. Muehlens,* District Court of Haarlem, 26 September, 1995, KG 1995, 384. These cases will be analyzed in the following section on termination disputes in the Dutch distribution system for luxury cosmetics.

initiated a summary procedure contending that the termination was null and void because the import ban on which the termination was justified infringed EU anti-trust law. At the same time he had also threatened to file a complaint with the EU Commission.

In contrast to the District Court which held for the importer, the Court of Appeal favoured the dealer. It concluded that the import ban violated EU anti-trust law and was therefore null and void. Accordingly, the dealer's breach of contract could not be a valid reason for the termination of the distribution agreement. It ordered the importer to supply the dealer.[103]

Finally, it is interesting to note that recently some important decisions have appeared where civil courts have decided on the issue whether a distribution agreement violated Article 81(1) of the EU Treaty or not.[104] Furthermore, in the last few years there has been an increasing tendency for litigants to invoke the nullity of a contractual provision on the ground that it is in violation of EU anti-trust law. This practice has increased since the enactment of the new Dutch Competition Act.

### *Dutch Anti-trust Law*

In order to secure supplies or to obtain compensation distributors can also make use of the private law enforcement of Dutch national anti-trust law. When the new Dutch Competition Act is violated distributors can directly invoke its provisions before the civil courts. They can invoke Article 6(2) of the new Dutch Competition Act which renders any agreements in contravention with Article 6(1) automatically null and void. In accordance with EU anti-trust law, the nullity does not in general extend to the whole agreement. Distributors can invoke the Article 6 in conjunction with Article 3:41 which provides for partial nullity.

However, generally speaking, similar problems for distributors exist as with the private law enforcement of EU anti-trust law. First, suppliers will usually not justify the unilateral termination with the non-compliance by the distributor of a forbidden trade practice. Second, most decisions in cases where the Act is invoked are delivered in expeditious summary procedures. Compared to the Dutch Competition Authority the Presidents of District Courts may lack sufficient expertise to apply the Act in these procedures. Usually, their knowledge lags behind that of the lawyers who may be involved in a large EU anti-trust law practice.

Nevertheless, when taking into view the strong indirect impact of the Act on civil disputes other than termination disputes, it may be assumed that the Act will also have a strong influence on disputes which have been caused by the termination of distribution agreements. In the first year after the enactment of the new Act, Presidents of District Courts have

103 *Coenders v. Nagel,* Court of Appeal of Arnhem, 14 April 1998, KG 1998, 148.

104 *Johnson v. Novem,* HR 20 November 1998, NJ 1999, 118. This case did not involve a termination dispute but a dispute in relation to the existence and validity of a non-competition clause.

rendered decisions on the new Act on approximately 40 occasions in summary procedures. After some initial errors[105] the quality of the decisions by the Presidents has improved.[106]

*Complaints to the Commission or to the Dutch Competition Authority*

– Complaint to the Commission

If EU anti-trust law should apply, distributors can also file a complaint with the Commission against the supplier which has terminated the contract.[107] However, the Commission is not bound to take up the complaint and initiate an investigation. This will usually depend on the priorities which have been set by the Commission. Furthermore, there is no specific time limit within which it is obliged to respond.[108]

In contrast to Japan, the complainant can file an appeal with the Court of First Instance when it does not agree with a formal decision of the Commission upon a complaint. Moreover, in some cases when the Commission has not initiated a case the complaint may also be filed with national competition authorities which are becoming increasingly important in enforcing EU anti-trust law.[109]

However, even if the Commission decides to investigate and finds an infringement of Article 81, this may not necessarily provide an immediate remedy for the distributor. This is because, similar to the FTC in Japan, the Commission cannot order the supplier to supply. Instead, the distributor usually needs a rapid interim measure which he can only obtain before a national court. Only indirectly the complaint may have some influence. When the Commission imposes fines or threatens to do so, the supplier may decide on its own initiative to supply the distributor in order to avoid the fines. Another reason for the complaint may be that important information can be brought forward by the Commission when it has initiated an investigation into the practices of the supplier. Although the Commission does

105 In one case which has been fiercely criticised by Dutch legal scholars the President of the District Court of The Hague rejected a request for an injunction on the basis that a similar provisional order could also be requested from the Dutch Competition Authority. *Campinggids/ANWB,* President of the District Court of The Hague, 10 July 1998. See *TVVS* 1998, p. 247. Sometimes the Presidents had been very reluctant to apply national anti-trust law, requiring the parties to await the decisions of the Dutch Competition Authority.

106 See F. J. Leeflang and K. J. M. Mortelmans (1999), 'Rechtspraak over de Mededingingswet in 1998' (Case law on the Competition Act in 1998), in: *Markt en Mededinging* 1999, p. 100.

107 According to Regulation 17 which consists of procedural rules to implement Articles 81 and 82 the opening of an investigation by the Commission may follow from a complaint by a company (Article 3).

108 See for example the decision of the Court of First Instance in *Guérin automobiles v. Commission,* 11 March 1996, Case T-195/95, [1996] ECR II 171. In this case a dealer had filed a complaint with the Commission against Volvo France SA which had terminated the distribution agreement. After 2 years the Commission had still not taken a decision and therefore the dealer appealed. The court confirmed EU case law that a complainant does not have the right to obtain a decision from the Commission.

not have to report all new information, some facts which have become public can be used as evidence by the distributor before a civil court.

However, it should be noted that there are many barriers for distributors to file a complaint such as time and costs. It is therefore not surprising that among distributors there is much reluctance to file such a complaint.

– Complaint to the Dutch Competition Authority

In the absence of any procedural rules on complaints in the Dutch Competition Act, the procedural rules for filing a complaint are governed by the General Act on Administrative Law. In principle, every citizen can file a complaint with the Dutch Competition Authority for a violation of anti-trust law but such request is dismissed if the person making the request is not directly concerned.

The reasons for distributors underlying a complaint may be similar to the reasons for a complaint being sent to the Commission. The Director General has a certain discretionary power of whether to take up a complaint, but a negative decision to that effect or a decision rejecting the complaint after an investigation is subject to appeal.

Generally speaking when taking into view all complaints filed so far, the Dutch Competition Authority has almost always rejected the complaints. Filing a successful complaint has proven to be very difficult. First, there is still some lack of transparency in the Dutch Competition Authority' policy as regards taking up complaints. Second, because of its enormous workload it must set priorities. Frequently, it explained the decision not to take up the complaint by stating that it was highly probable that the results of a possible investigation would show that no violation of the Act had occurred. It also sometimes added that it must set priorities. [110]

On a number of occasions distributors have filed complaints after distribution agreements have been terminated. In some of these cases they claimed that the termination had occurred because they resold at prices lower than those indicated by the supplier. In one case the Dutch Competition Authority decided in favour of the supplier, arguing that there was insufficient evidence that the supplies of the product were made dependent on whether or not the shop followed indicated resale prices.[111] By contrast, in another case it found clear evidence of price fixing contracts which were in violation of Article 6. In a formal decision it imposed an order under periodic penalty payments in which it demanded the supplier to remove the resale price maintenance clause from the standard-form distribution agreement.[112]

A much better option for the distributor might be the request for an order sanctioned by 'preliminary' periodic penalty payments *(voorlopige last onder dwangsom)* pursuant to Article 83 of the Act. If the Director General is of the provisional opinion that there is a

109 The new Dutch Competition Act offers the possibility to the Dutch Competition Authority to apply Articles 81 and 82 of the EU Treaty directly if the Commission has not initiated a case. In practice this has frequently occurred causing a great deal of extra work for the Dutch Competition Authority.

violation of Article 6 and Article 24 of the Act and immediate action is considered necessary in view of the interests of third parties or the interest of preserving effective competition, a provisional order with penalty payment may be issued in order to force the suspected undertakings to terminate certain conduct. In the Explanatory Memorandum to this Article the refusal to supply is named as one example of conduct which might lead to such interim relief. This means that the Dutch Competition Authority may require a supplier to resume supplies when he has violated the Act. In theory this may apply to cases where the complainant goes bankrupt if supplies are no longer delivered.

In one termination dispute a distributor requested such a provisional order after it had unsuccessfully initiated a summary procedure before a District Court. However, the Dutch Competition Authority refused to grant such an order. The reason was that it was not probable that the Act had been violated. Furthermore, there was no need for 'immediate' action.[113] Generally speaking, in actual practice such orders have been requested frequently but only once has the Dutch Competition Authority granted such an order.[114]

### *Chilly v. G-Star*

The following case deserves some detailed analysis. In this case both the Dutch Competition Authority and the civil courts were involved. As in many other cases the civil courts adhered more to contract law than to anti-trust law.

This case involved a dispute between an importer of jeans and seasonal collections of the G-star brand (hereafter G-Star) and a company which operates a number of stores where these G-Star brands are resold (hereafter Chilly). In the general conditions of contract G-Star had imposed a duty upon the purchasers of its products to only resell the products to individual customers. The contract provided a prohibition on reselling the goods to other outlets (retailers or wholesalers) without G-Star's prior approval.

After Chilly had regularly ordered these brands from G-Star for six years, it decided to open two more shops. G-star did not agree and notified Chilly that there were already sufficient outlets for the sale of its goods. G-Star thereby eventually refused to continue to supply Chilly. Chilly notified the latter that the prohibition on reselling to other outlets was in violation of the Dutch Competition Act and the EU Treaty. G-Star thereby responded that the acceptance of any orders did not fit within its distribution policy and argued that

110 See A.T.Ottow (1999), 'De Obstakels voor het indienen van een klacht bij de Nma' (The Obstacles for filing a Complaint with the Dutch Competition Authority), in: *Markt en Mededinging* 1999, p. 5–9; See also Ch. R.A.Swaak (1999), 'Het eerste jaar van ontheffingsaanvragen, bezwaren en klachten in Nederland' (The First Year of Complaints, Administrative Appeals and Notifications for Exemption), in: *Markt en Mededinging* 1999, p. 66–68.

111 Dutch Competition Authority Decision, *Leidse Stripshop v. PS Games,* 21 January 1999, No. 413.

112 Dutch Competition Authority Decision, *Free Record Shop v. Erasmus Muziekproducties,* 25 March 1999, No. 570.

the non-acceptance of the order was not related to the prohibition on reselling to other outlets.

Chilly first initiated a summary procedure and claimed that the termination was invalid in order to secure the supplies of the G-star brand. First, it contended that a distribution agreement existed between the parties. For such a long-term agreement the principle of good faith dictates that a reasonable advance notice must be provided. Second, it argued that the reason for the termination, non-compliance with the prohibition on reselling to other outlets, violated EU law and the Dutch Competition Act. However, the President of the District Court of Amsterdam rejected the claims of the plaintiff. The court based its decision on contract law, holding that no distribution agreement had existed between the parties which would establish a duty to accept each order from Chilly.[115]

However, on appeal the Amsterdam Court of Appeal pronounced judgement in favour of Chilly. Although it confirmed the District Court's view that no distribution agreement had existed, it held that G-Star had violated the principle of good faith. In view of the continuing relationship it was not free to reject the order because certain orders no longer fitted within its distribution policy. The court held: "Because of the continuing relationship and the fact that so far its orders have never been rejected, except for circumstances which are not applicable here, Chilly could rely on the acceptance of the order. Chilly's notification that the prohibition on reselling violated the new Competition Act does not constitute such a circumstance".[116]

The court had not referred to the issue of whether the prohibition on reselling violated Article 6 of the Dutch Competition Act or not. Just five days after the initial decision of the District Court of Amsterdam in the summary procedure, Chilly also filed a complaint with the Dutch Competition Authority.[117] At the same time Chilly also requested an order under 'preliminary' periodic penalty payments in which G-Star would be ordered to resume supplies. The Dutch Competition Authority, however, refused to grant the order.

First, it held that there was no longer any violation of Article 6 since the prohibition on reselling to other outlets had been removed from G-Star's general conditions by the end of March 1998. Second, the other requirement for such an order, the need for immediate action, had not been met. Chilly had not proved that in this case far-reaching irrevocable consequences would make it impossible to await the decision based on a normal procedure after a complaint.[118]

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113 See Dutch Competition Authority Decision, *Dutch Farm v. Dopharma International BV,* 3 August 1999, No. 1114; See also Dutch Competition Decision, *Polectro Plaza BV v. Bang & Olufsen Nederland BV,* 8 April 1998, No. 134.

114 Dutch Competition Authority Decision, *Audax v. Edipress,* 11 August 1998, No. 803. Audax had filed an administrative appeal *(bezwaar)* against this decision but this was rejected in a decision of 25 February 1999.

115 *G-Star v. Chilly,* District Court of Amsterdam, 14 May 1998, No. KG 98/1150 Odc (not reported).

116 *G-Star v. Chilly,* Court of Appeal of Amsterdam, 20 August 1998, No. 651/98 SKG (not reported).

## 4.5 Conclusion

In summary it can be concluded that there are many difficulties for distributors when invoking EU and Dutch anti-trust law before civil courts. The availability of expeditious summary procedures is a strong weapon for distributors, but at the same time the Presidents of District Courts find it difficult to apply anti-trust law in such procedures. They sometimes lack the required expertise to render decisions when the issues become very complex.

However, generally speaking, with the new Competition Act the civil courts are more involved in anti-trust issues than previously and the courts start delivering an increasing number of decisions in which EU or Dutch anti-trust law is applied. This may increase the possibilities for distributors to take on suppliers which have violated anti-trust law when they terminated a distribution agreement.

As regards the complaints with the EU Commission or the Dutch Competition Authority there are also many barriers for distributors. Immediate remedies are difficult to obtain. Although the Dutch Competition Authority may impose an order under 'preliminary' periodic penalty payments, urging a supplier to resume supplies, it is still very reluctant to do so.

Furthermore, it is difficult for distributors to gather sufficient proof of any violation of EU or Dutch anti-trust law. As regards time and costs a complaint with the Dutch Competition Authority may be more favourable than a complaint with the EU Commission but, in general, so far the Dutch Competition Authority has rejected most complaints.

The reason why complaints are usually not successful may also partly be due to the enormous workload of both the EU Commission and the Dutch Competition Authority which requires them to set priorities. For example, The Dutch Competition Authority has received more work than anticipated and it has already increased its staff from 80 to 120 officials.

Finally, as regards the relationship between the Dutch civil courts and the competition authorities the following can be concluded. The relationship with the Dutch Competition Authority is not yet fully clear but this may be explained by the fact this Authority has only recently been established in 1998. Gradually the relationship between the civil courts and this Authority will become clearer. So far, the decisions of Presidents of District Courts in summary procedures may have exerted some influence in procedures before the Dutch Competition Authority.[119] The Dutch Competition Authority also in fact encourages complainants to initiate procedures before the civil courts.[120]

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117 On 30 December 1998 the Dutch Competition Authority had issued the report, which precedes a decision, in which it had concluded that many clauses in G-Star's general conditions had violated Article 6 of the Act. It held that a fine and an administrative order with periodic penalty payments must be imposed. G-Star must inform all its distributors that they can sell the products to every retailer and at the resale price they want. In addition, G-Star must clearly motivate any refusal to supply a retailer which had ordered the Jeans for more than three subsequent years.

118 Dutch Competition Authority Decision, *Chilly v. G-Star,* 7 August, 1998, No. 758/26.

In turn, so far there have been few cases in which civil courts have referred to procedures and decisions of the Dutch Competition Authority. For example, in the case described above between Chilly and G-star the civil courts did not refer to the complaint and the request for an interim relief by Chilly. Evidently, the relationship between the Dutch civil courts with the EU Commission and Community Courts is clearer partly for the simple reason that the latter have rendered more formal decisions. In general, Presidents of District Courts often refer to these decisions when they apply EU law. In turn, a decision of the civil courts in which it is stated that EU law is violated can be an important piece of evidence to be used when filing a complaint with the Commission.

Generally speaking, both the EU Commission and the Dutch Competition Authority actually encourage the use of civil courts to invoke anti-trust law.

*Comparison with Japanese Law*

Comparing applicable anti-trust law in the Netherlands with anti-trust law in Japan leads to the following conclusions.

One similarity in both countries is that increasing importance is being attached to the private law enforcement of anti-trust law. Both the stricter application of Japanese anti-trust law and the establishment of the new Dutch Competition Act falling into line with EU law have proven to affect the private law enforcement of anti-trust law. This may also affect the possibilities for distributors to take on suppliers which have violated anti-trust law when they terminated a distribution agreement.

Nevertheless, in both countries there are many difficulties for distributors to invoke anti-trust law. For comparable reasons both in the Netherlands and in Japan the civil courts find it difficult to apply anti-trust law and they rather justify their decisions on contract law.

Compared to Japanese distributors, however, Dutch distributors have more possibilities by means of the expeditious summary procedures. Presidents of District Courts start to become more familiar with complex issues of anti-trust law.

As regards the filing of complaints there are also comparable difficulties although in the Netherlands, the decisions of the Dutch Competition Authority not to take up a complaint or to reject the complaint are subject to appeal.

One important difference with Japan is that EU and Dutch anti-trust law provide more clarity concerning what kind of actions are in violation of these laws. This is caused by the stronger and more formal enforcement of anti-trust law by the Commission, the Community Courts and the Dutch Competition Authority. The forthcoming new single umbrella Block Exemption Regulation may only increase this clarity.

Furthermore, the relationship between anti-trust law and other laws is more clearly defined in the Netherlands. For example, the relationship with the Civil Code is much

119 See for example the Dutch Competition Authority decision, *Dutch Farm v. Dopharma International BV,* 3 August 1999, No. 1114.

120 See Ch. R.A.Swaak (1999), o. c., p. 71.

clearer by means of Article 81(2) of the EU Treaty and Article 6(2) of the new Dutch Competition Act which automatically render a contract (clause) in violation thereof null and void. By contrast, in Japan such provisions do not exist.

The same applies to the relationship between anti-trust law and civil procedural law. It is evident that the EU Commission and Dutch Competition Authority more actively encourage the use of civil courts to enforce anti-trust law.

## 5
## APPLICABLE CONTRACT LAW AND EU ANTI-TRUST LAW IN THE DUTCH DISTRIBUTION SYSTEM FOR LUXURY COSMETICS

### 5.1
### Introduction

The purpose of this section is to briefly study the role of contract law and anti-trust law, as described above, in one particular industry in the Netherlands. I have chosen the distribution system for luxury cosmetics because it is comparable to the system in Japan which I have already described.

The distribution system for luxury cosmetic products in the Netherlands shares certain characteristics with the Japanese distribution system. In the Netherlands luxury brands are mainly distributed through subsidiaries. Manufacturers have usually established a subsidiary in the Netherlands through which the luxury cosmetic products are sold to selected retail outlets.[121] Sometimes manufacturers also distribute their goods to these selected retailers through the intermediary of an independent Dutch company acting as the exclusive importer. Generally speaking, the retailers must meet certain conditions in order to reflect the prestige of the luxury brand.

In this section I will start by providing some general background information on the frictions between cosmetics manufacturers and discounters in the Netherlands which started in an earlier period and generated different legal disputes than in Japan. Subsequently, the current relationship between subsidiaries/exelusive importers and their selected retailers within the Netherlands is described, which includes a study of their contractual relationships.

Finally, I will refer to a certain extent to the terminations of the distribution contracts by subsidiaries/exclusive importers and the subsequent response of the selected retailers. As in Japan unilateral terminations of distribution agreements occur regularly, but they seldom lead to litigated termination disputes.

In this section my main emphasis is on applicable Dutch contract law and the private law influence of EU anti-trust law. In relation to the distribution of luxury cosmetics the role of national Dutch anti-trust law is limited. This is because large manufacturers of luxury cosmetics use similar selective distribution systems in many EU countries. This means that trade between Member States is affected and EU law is thereby applicable.

Because the number of reported termination disputes within this industry is very limited there was an even stronger need for supplementary sociological information that allows us to evaluate the significance of these cases. I proceeded by gathering standard-form contracts and conducting interviews with a general director of the Benelux sales company of Christian Dior and two lawyers who specialise in legal disputes within the cosmetics industry.[122] Furthermore, I collected general background information from the industry itself such as reports. Although this description of actual 'living' law in the Dutch cosmetics distribution will not be as detailed as the analysis of the similar industry in Japan, it may still function to bring my findings in Japan into perspective.

## 5.2
## Different Legal Disputes to those in Japan

Legal disputes between manufacturers and retailers in the Dutch distribution system for luxury cosmetics have not necessarily been caused by unilateral terminations of distribution agreements by manufacturers.

It is important to realise that in the Netherlands discounters and manufacturers had already started taking on each other in the late 1970s. In contrast to the disputes between Japanese manufacturers and retailers, which started at the end of the 1980s, disputes between manufacturers and retailers in the Netherlands started much earlier. In the late 1970s manufacturers of luxury cosmetics wanted to make their distribution system more selective and started to limit the number of outlets. This period saw the emergence of the selective distribution systems for luxury cosmetics. At the same time parallel traders and large retail drugstore chains selling at discounts started challenging the selective distribution systems. However, this did not necessarily trigger termination disputes since they were almost never admitted into the authorised retail network. They purchased luxury brands from outside the network.

Two typical sorts of legal disputes started to appear. First, manufacturers of luxury brands initiated a summary procedure in order to stop these large retail drugstore chains and parallel traders from reselling their products which they had obtained from outside the authorised retailer network. These cases were often appealed and led to a number of Supreme Court decisions which generated much publicity. In these cases the manufacturers usually lost.[123] It is interesting to note that during the course of these disputes the Dutch District Courts on some occasions decided that in general the selective distribution system for luxury cosmetics is incompatible with Article 81(1) of the EU Treaty.[124] However, these are exceptional cases. In most cases the Dutch courts have accepted the selective

121 Almost all the manufacturers are from outside the Netherlands. Most of them are French.

distribution system with the application of the criteria of the decisions of the Court of Justice.[125]

Another typical kind of common dispute was initiated by companies which tried to gain admittance to the network. For example, some larger firms such as the mail-order firm, Otto, were denied admittance to the network. In response, Otto litigated as far as the Dutch Supreme Court, but without success.[126]

These frictions between the manufacturers, on the one hand, and the large discount drugstore chains and parallel traders, on the other, continued until approximately the late 1980s. After that the large chains started to reach some degree of understanding with the manufacturers and upgraded some of their stores in order to meet the qualitative criteria which had been set by the manufacturers of the luxury brands.

Currently some branch stores and franchisees of a large drugstore chain, Etos, have been selected as an authorised retailer by a number of luxury cosmetics manufacturers. This drugstore chain, purchased by the large Dutch concern, Ahold, had been the first to challenge the selective distribution system before the Dutch courts, but has now become less active in the field of litigation. In addition, the discount chain Paris XL, taken over by the large drugstore chain, Kruidvat, is currently opening many stores in the Netherlands. The large manufacturers of luxury brands have concluded authorised retailer contracts with those stores. In some cases selected retailers were simply taken over by the drugstore chain without any changes to the store. This meant that qualitative criteria were still being met, making unilateral terminations very difficult for the manufacturer.

Furthermore, parallel traders have also become less active in the field of litigation. Gradually, the selective distribution systems have become more closed as far as parallel traders are concerned which makes it very difficult for them to obtain luxury brands. Some have been declared bankrupt.

In conclusion we can summarise by saying that selling at discount prices and parallel trade are no longer a major cause for frictions between manufacturers and some large retailers. Currently the only frictions which remain are those between manufacturers and retailers which are not admitted to the network although they claim to meet the current selection criteria. Furthermore, there are still frictions between manufacturers and retailers which have been removed from the network because they do not meet the qualitative selection criteria or do not attain the minimum annual purchase figures. However, such frictions seldom lead to litigated disputes.

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122 Interviews were conducted with G.van der Wal, representing the L'Oreal group and with R.F.K. Visser, representing the interests of many distributors and parallel traders. I asked them about their experiences with termination disputes.

123 See, for example, *Cacharel v. Geparo,* HR 1 November 1991, NJ 1992, 423; *Christian Dior v. Kruidvat,* HR 20 October 1995, Rvdw 1995, 212C; *Cacharel v. Trade Max,* HR 1 November 1991, NJ 1992, 424.

124 See for example District Court of Haarlem, 4 April 1984, KG 1984, 143.

The few litigated termination disputes which led to decisions by the Presidents of District Courts in summary procedures in the 1990s, which will be described later, must therefore be viewed as exceptional cases.

## 5.3
## The Distribution System for Luxury Cosmetics in the Netherlands

As in other EU countries, in the Netherlands the current system of selective distribution in the cosmetics industry originated in the 1970s. In the Netherlands around 20 to 30 percent of all cosmetic products are distributed through authorised retail networks. This applies to luxury cosmetics which are distributed through similar networks as those used by large manufacturers in Japan. Large manufacturers such as Chanel, Christian Dior, Givenchy and Lancome have an authorised retail network for the sale of their luxury cosmetics. These manufacturers have a large degree of control over the selected retailers. First of all by using qualitative criteria they aim to make use of only qualified retailers and to limit the number of outlets.[127] Furthermore, they adopt standard-form contractual provisions which impose many duties upon the retailers.[128]

In contrast to the overwhelming market share of Shiseido within Japan, there are no manufacturers which hold an absolute leading market share of luxury cosmetics in the Netherlands. The leader is Lancome which currently has around 10 percent of the market share for luxury cosmetics. On average these producers use approximately 300 selected retailers to distribute their products.

Among the total number of selected retailers within the Netherlands, approximately 300 are perfumeries with a very luxurious image. They are dependent on luxury cosmetics for a very large percentage of their product line.[129] Luxury brands are also distributed through drugstores, which do not usually have such a luxurious image, but can still be selected as an authorised retailer. Luxury brands account for only a small percentage of the total turnover of these drugstores. However, drugstores, which have become branch stores of rapidly growing discount drugstore chains, have so far seldom been admitted to the network.[130] As mentioned above, only a few 'Etos' and 'Paris XL' stores have been selected as a retailer by some manufacturers of luxury brands. Finally, as in Japan, many luxury brands are distributed through selected department stores.[131]

125 See Case 99/79, *Lancome v. Etos* [1980] ECR 2511 and Case 31/80, *L'Oreal v. De Nieuwe AMCK* [1980] ECR 3775. See also the Commission's decisions: *Yves Saint Laurent Parfums,* 16 December 1991, O. J. 1992 L 12/24; and *Parfums Givenchy,* 24 July 1992, O. J. 1992 L 236/11; and the decisions of the Court of First Instance in Case T 19/92, *Leclerc v. Commission* [1996] ECR II 1851; Case T 87/92 *Kruidvat v. Commission* [1996] ECR II 1931 and Case T 88/92, *Leclerc v. Commission,* [1996] ECR II 1961.

126 See for example, *Christian Dior v. Otto,* HR 13 December 1991, NJ 1992, 588.

*The Relationship between the Subsidiary/Exclusive Importer and the Selected Retailer*

As in Japan, the selected retail outlets are highly dependent on the supply of each luxury brand they resell. Although they usually resell many competing luxury brands, the halting of supplies of one brand may harm their corporate image considerably. In such cases other manufacturers may also decide to stop supplying the retailer. Furthermore, the contractual provisions impose upon the retailer an obligation to resell 'sufficient' brands of a 'comparable' reputation. This means that the loss incurred after halting supplies may be comparable to the loss incurred by selected Japanese retailers when the supplies of one brand have been stopped.

As in Japan, there are many business practices used by the manufacturers which strengthen the dependence of the retailer upon the manufacturer. They offer wide-ranging support to their selected retailers and various services are provided in order to maintain control over channels. These are performance-related bonuses,[132] marketing advice, promotional activities and various forms of financial assistance. In order to provide these services representatives from the manufacturer regularly visit the retailer. These services are, however, not included in the standard-form authorised retailer contracts which establish the relationship between the manufacturer and the selected retailer.

– Standard-form Contracts

As in Japan the balance of power is in favour of the manufacturers, which is illustrated by the provisions of the standard-form contract. These contracts impose many obligations upon the retailer in order to maintain the prestige brand name of the luxury cosmetics. They stipulate explicitly that the retailer has to refrain from selling by mail order or to resell to retailers or wholesalers outside the authorised retailer network.

However one difference with the Japanese contracts is that an obligation is imposed upon the retailers to achieve a minimum amount of annual purchases. This is to be set out in a separate letter, or attached to the contract and must be signed by both parties. Retailers who fail to achieve this amount are often excluded from the various services provided by the manufacturers. For example, the important regular visits by the manufacturer's

127 This may be difficult since EU law requires an open system which means that all qualified distributors must be accepted. Adjusting and toughening the qualitative criteria does not always have an impact on the number of distributors. Making the criteria stricter also necessitates that all existing outlets will meet the new criteria. EU law requires uniform criteria which have to be applied without discrimination to new and existing outlets alike.

128 See the report from A.P.Weber (1988), *'Les systèmes de distribution selective dans la communauté du point de vue de la politique de concurrence—le cas de l'industrie des parfums et des produits cosmetiques'*, p. 102–103.

129 W.V.M.van Rijt-Veltman (1994), *Parfumeriespeciaalzaken,* Research by EIM Centrum voor Retail Research, p. 11.

130 Ibid., p. 12.

131 Ibid., p. 13.

representatives are not continued. In most cases these stores are gradually removed from the network.

As in Japan, all standard-form contracts are concluded for one year, being automatically renewable for one further year unless any of the parties gives notice of an intention to terminate at least a few months before the end of the contract. Furthermore, these contracts stipulate that the producer has the right to terminate immediately if the retailer has breached any material terms of the contract. These material terms include the obligation not to resell the cosmetics to other retailers or wholesalers, which have not been admitted to the network.

Generally speaking, these standard-form authorised retailer contracts are longer and more detailed than those in Japan. In contrast to the Japanese contracts, in the Netherlands in most cases the general conditions of sale and the selection criteria are attached to the contract. Manufacturers also usually make use of comprehensive checklists for internal use, setting out the requirements which the retailers must meet. The use of detailed selection criteria within these lists can be explained by the influence of decisions of the EU Commission and the Community Courts.

When producers in Europe first started to use authorised retail networks in the 1970s, the EU Commission did not interfere to any great extent in these contracts. It had delivered many 'comfort letters' to the large producers. However, the Commission changed its attitude at the beginning of the 1990s after the very influential report by Weber, which had been initiated to investigate selective distribution agreements in the cosmetics industry.[133] The Commission found that in selective cosmetics retailer networks there could be a clear restriction of competition. Standard-form contracts had to be sanctioned by the Commission and these were considered as an example for other producers. For example, in the Commission's Yves Saint Laurent decision the standard-form contracts, which were in use, were amended.[134] This had a great deal of impact and many producers started to check their contracts with the Commission for any necessary amendments. In most cases the leading producers have not changed their contracts since then. Differences are mainly seen in the selection criteria adopted by each manufacturer, which have become more detailed than previously.

132 For example, the 'Year end bonus', to be determined in proportion to the amount of goods purchased by the retailers.

## 5.4
## Unilateral Termination of Distribution Agreements

*Unilateral terminations*

Within the luxury cosmetics industry unilateral terminations of distribution agreements have occurred regularly. For example, at the end of the 1980s Lancome changed its sales policies in order to gain a more luxurious image. It decided to extensively reduce its number of around 1500 selected retailers in the Netherlands. It started to terminate contracts with retailers who had not achieved the required minimum amount of annual purchases. It has currently reduced the number of selected retailers to around 600. In most cases the Dutch subsidiary of Lancome gradually wound down the ongoing relationship and steadily reduced the volumes transacted. Retailers who did not achieve the required minimum amount of annual purchases were put on so-called '99-lists'. This meant that the regular visits by Lancome's representatives to these stores would stop. This system was established in order not to terminate contracts abruptly.

Lancome usually terminated the authorised retailer contract with a few months' notice. In a final visit by such a representative the reasons for the termination were explained. In most cases the retailer did not initiate any legal action. Frequently they realised that any extension of the contractual relationship was difficult since they could no longer afford the necessary investments. However, some which had taken out insurance cover for litigation costs called on the services of a lawyer. In these cases they usually invoked EU anti-trust law, asserting that the criterion for termination was not valid, since it violated Article 81 (1) of the EU Treaty.[135]

However, most retailers did not proceed with legal action. According to the lawyer representing the L'Oreal group he had not experienced any litigated termination dispute for the last 10 years.[136]

Other manufacturers such as Chanel, Dior and Lancaster have also regularly terminated contracts with specialised retailers, but less frequently than Lancome. Usually the disclosed reason for termination was also that the retailer had not achieved the required minimum amount of annual purchases. Those who called in a lawyer often also invoked Article 81(1) of the EU Treaty, asserting that the reasons for cancellation were not valid.

The threat of invoking anti-trust law before a civil court has sometimes proved to be very effective. In some cases manufacturers have reconsidered their expressed intention to terminate after the selected retailer had threatened to initiate a summary procedure. In one recent case a subsidiary had expressed its intention to cancel the agreement with a retailer who had achieved annual purchases of Dfl. 80,000. However, the retailer effectively asserted that its amount of annual purchases had exceeded 40 percent of the average purchase figure, during the previous year, of all the retail outlets concerned. This meant that the

133 See the report from A.P.Weber published in 1988 by the Commission.

134 See *Yves Saint Laurent Parfums,* 16 December 1991, O. J. 1992 L12/24.

subsidiary could not justify its termination by invoking the non-achievement of a minimum annual purchases requirement.[137] Eventually the subsidiary decided not to terminate.[138]

However, in most cases retailers are quite reluctant to initiate legal proceedings since the litigation costs may be prohibitive. Furthermore, gathering evidence to prove that there has been a violation of EU anti-trust law might be too difficult and costly.[139]

By contrast, retailers who have not been admitted to the network have usually invested a great deal of money in order to meet the qualitative criteria and they may go further in challenging the manufacturers. In some cases manufacturers have reluctantly admitted retailers who have met the qualitative selection criteria completely and have threatened to initiate a summary procedure.[140]

Finally, another option is to file a complaint with the Commission or to threaten to do so. However, there is much reluctance among distributors to file a complaint with the Commission in Brussels. It is seen as expensive to go to Brussels and it takes too much time for them to gather sufficient evidence in order to point to a violation of EU law by the manufacturer. Distributors prefer summary procedures to such complaints. It should also be noted that when the President of a District Court has applied EU law in favour of the distributor it becomes easier for the distributor to file a complaint with the Commission, because he can use the civil court decision as evidence. For this reason manufacturers fear such decisions the most.

Generally speaking, the incentives to unilaterally terminate contracts with retailers may have increased. One of the reasons is that in some cases it has become difficult to refuse stores admittance to the network when they are able to meet all the qualitative criteria. Therefore, the number of retailers included in the network may have become higher than intended by the manufacturer. The latter tries to limit its number of selected retailers in order to maintain its luxury image. Therefore, some manufacturers have recently upgraded the qualitative criteria, which enables them to terminate their agreements with stores which cannot meet such higher criteria.[141]

135 R.F.K. Visser, Personal communication, 12 February 1998.

136 G.van der Wal, Personal communication, 5 March 1996.

137 In the Yves Saint Laurent decision the Commission held that the minimum annual purchases requirement cannot exceed 40 percent of the average purchases figure, during the previous year, of all the retail outlets concerned.

138 R.F.K. Visser, Personal communication, 12 February 1998.

139 Ibid.

140 Ibid.

*Litigated Termination Disputes*

In the Netherlands termination disputes such as in the Japanese distribution system for luxury cosmetics, which have been described in detail in chapter 4, have not occurred.

In contrast to the Japanese disputes which continued all the way up to the Supreme Court, in the Netherlands they all involve decisions of Presidents of District Courts in summary procedures, which were not followed by full procedures or appeals and were therefore final. As explained previously, these cases which occurred in the 1980s and 1990s must be viewed as exceptional and they by no means represent the general frictions between manufacturers and retailers which started in the late 1970s. Nevertheless, they can provide an insight into the role of contract law and anti-trust law when such summary procedures are initiated.

One reason for these cases to end up in court may be that in almost all of them the supplier had terminated with immediate effect, leaving the distributor with no choice but to litigate. In these cases the distributors demanded specific performance of the contract and asserted that the termination was not valid since it breached the principle of good faith.

In the following case anti-trust law was irrelevant and was also not relied upon by the distributor. Only matters of contract law were at issue. In this case the court emphasised, in a very influential decision, the dependent position of the selected retailers.

*– Chanel v. Oosenburg*

This termination dispute started after the exclusive importer of Chanel brands had terminated the contract with a selected retailer/drugstore. Six years into the agreement it suddenly terminated for no stated reason and gave two months' notice. In court it appeared that the supplier had terminated because the drugstore had regularly been late with its payments. Furthermore, in view of its limited turnover during the last few years it had not put enough effort into selling Chanel products. The President of the District Court of The Hague adjudged this termination to have breached the principle of good faith and ordered the importer to supply the drugstore.

The court held: "The termination of a continuing contract such as this agreement is so influential that it may not occur without prior warning and without disclosing a reason therefor". Although the drugstore had indeed regularly paid too late, the supplier had never warned the drugstore that this could be a reason for termination. Furthermore, there was no provision in the contract about the required turnover and the importer had not previously indicated that an insufficient turnover could lead to termination. The supplier had even admitted that it also continued contractual relationships with retailers which did not make a profit, making the said termination very arbitrary and therefore invalid.

141 Ibid.

The court added an important factor by explaining that the termination was very damaging for the drugstore. It lost its position as a selected retailer for Chanel products and was unable to reestablish such a position because the supplier was the exclusive distributor of Chanel products. Although the drugstore could obtain Chanel brands from other sources, this would harm its usual profit margin.[142]

In the following case a selected retailer had successfully invoked EU anti-trust law before the President of the District Court.

### – *Devecos v. Drogisterij Shalom*

In this termination dispute an exclusive importer of many luxury brands had concluded an authorised retailer contract for the sales of one brand with a drugsto-re/perfumery. Four years into the agreement the importer cancelled the contract with immediate effect after the drugstore had moved to a different location. The importer justified the cancellation on the clause in the contract, which stipulated that the supplier had the right to terminate with immediate effect if the retailer did not meet any of its obligations. The retailer had repeatedly notified the supplier that it was about to move but the importer had responded neither negatively nor positively. When the retailer demanded the supplies of the cosmetics to its new store, the importer refused on the ground that the retailer had started to sell the cosmetics at the new store without the required prior consultation. The drugstore responded by initiating a summary procedure claiming specific performance and asserting that the termination breached the principle of good faith. In addition it held that the behaviour of the importer infringed Article 81(1) of the EU Treaty.

The court held in favour of the plaintiff and decided that the immediate termination had violated the principle of good faith. There was no urgent reason to justify immediate termination. The court found it to be of importance that the importers' ambiguous attitude had led the drugstore to expect that the relationship would continue. Furthermore, the importer could have made use of the contract clause, which stipulated that the contract could be terminated with a three-month notice period.

In relation to the violation of EU anti-trust law the court held that the importers' arguments were not valid. In court the importer had argued that it had not yet completed a renewed procedure for admission, necessitated by the change in the store's location. However, the court held that the geographical location of the store could not be a factor in the admission procedure of the retailer pursuant to the decision of the Court of Justice, in which it was held that a selective distribution system is allowed only in so far as objective criteria of a qualitative nature are maintained.[143] The District Court ordered the importer to supply the cosmetics to the retailer.[144]

142 *Oosenburg v. Vermeulen,* District Court of The Hague, 1 September 1987, KG 1988, 293.

The following two cases did not involve a termination dispute between a subsidiary or exclusive importer and a selected retailer, but they are important in order to illustrate the reluctance of the Presidents of District Courts to apply EU anti-trust law.

### – *Helena Rubinstein v.Devecos*

This termination dispute involved an exclusive importer of many luxury cosmetics brands in a dispute with the French manufacturer, Helena Rubinstein *(HR)* from the L'Oreal group, from which it obtained its brand on an exclusive basis. In 1992, the importer started to sell *HR* products at discount prices in order to improve its diminishing turnover. After the importer resisted strong appeals to stop discounting, *HR* cancelled the agreement with 30 days' notice pursuant to the termination clause which enabled such a termination if the distributor defaulted in performing any material term of the agreement. It justified the termination by claiming that the distributor had violated the contractual obligation to maintain prices, which were concurrent with the image of the luxury *HR* brands.

The importer responded by initiating a summary procedure claiming specific performance of the contract. He argued that the termination was invalid because there was no valid reason therefor. He contended that there were no contractual provisions on which *HR* would be entitled to determine the resale prices of its products and added that it had not maintained such a price policy that would be harmful to the *HR* brand. Furthermore, he argued that Article 81(1) of the EU Treaty prohibits the supplier to determine resale prices directly or indirectly or take any measure, which would lead to such an impediment of competition.

The most important issue in this case was whether the reason for the cancellation was valid. The District Court ruled in favour of the plaintiff, holding that offering slight discounts did not damage the brand name and did not therefore violate contractual provisions. The court held that there was no valid reason to terminate and ordered *HR* to keep supplying Devecos.[145] The court only applied contract law by which to justify its decision.

### – *Muehlens v. Etos*

In this case between an importer of many luxury brands and an Etos discount drugstore the court also based its decision solely on contract law. In this case the two parties had not concluded an authorised retailer contract but over 10 years the Etos store had received annual price-lists with general conditions of sale and had subsequently ordered the luxury cosmetic products.

When the Etos store started to lower prices as part of a special sales campaign, the distributor stopped supplying the store, reasoning that it was not allowed to resell below recommended resale prices. Thereupon, the Etos store commenced a summary procedure

143 Case 99/79, *Lancome v. Etos,* [1980] ECR 2511.

144 *Drogisterij Shalom v. Devecos,* District Court of Haarlem, 3 July 1985, KG 1985, 248.

and demanded the deliveries which were still on order during that year. According to the store there existed a distribution agreement of an indeterminate period, which had been terminated without valid reason and without sufficient advance notice.

The store also argued that selling below recommended resale prices couldn't be a valid ground for termination because the recommended prices cannot be binding pursuant to the contract. Furthermore, it contended that pursuant to Article 81(1) of the EU Treaty a contract clause, which determines that products may not be resold below a certain minimum price, is null and void.

The District Court ruled in favour of the Etos store. Although it agreed with the defendant that there was no formal distribution agreement it held that changing resale prices did not constitute a sufficiently serious reason to withdraw the offer. However, the Court did not make use of the potential infringement of EU law in order to justify its decision.[146]

## 5.5 Conclusion

The relationship between the subsidiary or exclusive importer and the selected retailers in the distribution system for luxury cosmetics in the Netherlands is comparable to the relationship between sales companies and retailers in Japan. In both systems the manufacturers make use of many business practices, which strengthen the dependence of the retailer upon the manufacturer.

Furthermore, as in Japan standard-form contracts play a very important role in maintaining control over the retailers. One difference is that the standard-form contracts used in the Netherlands are longer and more detailed than those in Japan. One reason may be that the large French manufacturers use similar standard-form contracts in many different EU countries. This enhances the need for more detailed contracts.

Furthermore, this may in part also be attributable to the more defined rules of EU anti-trust law on selective distribution systems as set out in a large number of decisions by the Commission and the Community Courts. For example, the rules on selective distribution agreements require the manufacturers to use objective selection criteria. Accordingly, these criteria have been carefully drafted and have been appended to the contract. Moreover, in the Netherlands the selection criteria have become increasingly detailed in order to limit the number of retailers and to create possibilities to terminate the agreements with retailers which no longer meet these criteria.

These more defined rules of EU anti-trust law on selective distribution systems are not only attributable to the stricter enforcement of anti-trust law by the Commission but also to a greater number of formal decisions. These decisions are mostly the result of the legal

145 *Devecos v. Helena Rubinstein,* District Court of Haarlem, 24 July 1992, No. 1597/1992 (not reported).

146 *Muehlens v. Etos,* District Court of Haarlem, 26 September 1995, KG 1995, 384.

disputes which have been caused by the many challenges to these systems by those outside the network, such as large discount chains.

By contrast, the Japanese distribution system for luxury cosmetics has not faced that many challenges and there have been less legal disputes. The only serious challenges to the system started in the 1990s and came mostly from within the network. However, as is the case in the Netherlands these challenges from the discounters caused manufacturers to amend their standard-form contracts and to draft them more carefully.

Generally speaking, selected retailers in the Netherlands have more weapons to take on manufacturers than the selected retailers in Japan. The insurance cover for litigation costs and the availability of the expeditious summary procedure may mean that the threat to commence proceedings is more influential than in Japan. Manufacturers do sometimes give in to retailers because they do not wish to see the development of case law, which would make it more difficult to terminate the authorised retailer agreement.

The potential violation of anti-trust law has a great deal of impact in these termination disputes. Manufacturers are careful to call upon objective qualitative selection criteria in order to justify any termination. In this respect EU law is stricter than Japanese law. In contrast to manufactures in the EU countries, Japanese manufacturers are not bound to call upon objective qualitative selection criteria in order to justify a termination or to deny any request for admittance to the network.

Nevertheless, it must be noted that it is also very difficult for Dutch retailers to gather sufficient evidence to prove that EU anti-trust law has been violated. Complaints to the EU Commission also prove to be difficult.

Within the Dutch distribution system for luxury cosmetics there have been very few litigated termination disputes before the Dutch civil courts. This may be partly due to the fact that manufacturers have not usually terminated the contracts abruptly. Furthermore, as in Japan it is not easy for small distributors to take on powerful large manufacturers.

The few cases which have ended up in court are those where the manufacturer had terminated contracts very abruptly. In most of these decisions by the Dutch District Courts a good reason for such immediate termination was required and the retailer was protected. These cases also show that although the retailers often invoked EU law, the Courts did not usually refer to this law. They based their decisions primarily on contract law.

# 6
# A Discussion on Japanese Attitudes toward Contracts

## 1
## INTRODUCTION

There has been a very lively discussion on Japanese attitudes toward contracts among Japanese legal scholars and practitioners, which started in the 1960s with a famous work by the Japanese legal sociologist, Takeyoshi Kawashima. At the beginning mainly Japanese legal scholars and practitioners participated in this discussion but over the years many foreign experts on Japanese law and practice have joined in.

A major issue has been whether or not there are distinctive Japanese attitudes toward contracts, and if so, whether or not such attitudes are mainly due to cultural factors, such as a distinctive Japanese concept of the contract or not. At the beginning of this discussion, most legal scholars focused their attention on cultural factors, which shape Japanese attitudes toward contracts. Japanese contracting practices were mainly contrasted with contracting practices in the 'West', and in order to explain the distinctive Japanese characteristics, these scholars mainly directed their attention towards Japanese culture.

However, over the years an increasing number of legal scholars started to raise doubts about the existence of distinctive Japanese contracting practices and a distinctive Japanese concept of the contract. Even if they recognised distinctive Japanese features, they no longer explained them as being due to cultural factors. Many started to emphasise other factors which shape Japanese attitudes toward contracts. These include factors such as the nature of the legal system and the role of the Civil and Commercial Codes. Furthermore, the nature of trade relationships and the differences in bargaining power between contracting parties came more into focus.

This discussion between legal scholars and practitioners who place emphasis on cultural explanations and those who are critical of this continues to this day. In order to clarify this dichotomy, I will refer to some important representatives of both schools.

Within this discussion a great deal of attention has been directed towards the role of contracts and contract law in continuing trade relationships between Japanese companies. Many Japanese and foreign legal scholars have studied Japanese domestic commercial relationships in order to draw conclusions concerning Japanese attitudes toward contracts.

Since this dissertation deals with distribution agreements as a particular type of continuing contract it is hoped that it will contribute to that discussion. After reviewing some influential contributions to this discussion, I will summarise my findings, which are based on my study of Japanese contract law and anti-trust law, the field research within the Japanese distribution system for luxury cosmetics and a comparison with Dutch law and practice.

## 2
## THE EMPHASIS ON CULTURAL FACTORS

The cultural explanations were most prevalent during the 1960s and 1970s but are still very influential. Many Japanese and non-Japanese legal scholars and practitioners still believe that the law is largely irrelevant to Japanese contracts. They argue that for the Japanese the business relationship is most important. The Japanese favour unwritten or very brief contracts. They do not regard themselves as being bound by the letter of such agreements but rely instead on the flexible attitude of the other party to seek renegotiation. If a dispute arises, they will rarely allow the matter to proceed to court.

Most earlier studies were sweeping comparisons of Japanese contracting practices with those in 'the West', usually a reference to the US, which emphasised that the distinctive features in the two systems could be attributed to a different concept of the contract. Many scholars emphasised that the Japanese concept of the contract was 'unique' and somehow linked to the genesis of Japanese society.

### *Takeyoshi Kawashima*

The most influential scholar characteristic of this approach is the legal sociologist Takeyoshi Kawashima. In his chapter on contract consciousness in his work *Nihonjin no hōishiki* (The Legal Consciousness of the Japanese),[1] Kawashima focuses on the distinct nature of Japanese contracting and compares it with the formality of transactions in the West. In his model, harmony and trust in the relationship result in a more flexible attitude toward contract formalities. Not only are there many occasions where written agreements are not drafted, but even when these are drafted their contents are usually very simple and include only the most important elements. Moreover, even if detailed provisions are inserted in the contracts, they do not have much significance. The Japanese believe that even the rights and obligations provided for in the written agreement are tentative rather than definite. When a dispute arises the Japanese think it desirable at that time to fix the rights and duties by means of ad hoc consultation.

Kawashima illustrated this by pointing to the widespread use of 'confer in good faith' clauses in Japanese contracts. He used these clauses as an important example of the difference between the Japanese and the Western concept of the contract.[2] Kawashima argued that because of this distinctive Japanese concept of the contract, judicial protection for contractual claims cannot be considered important and the function of litigation in Japan has been distorted as a result.[3]

However, it is important to note that Kawashima focused his attention on the 'pre-modern' attitude of the Japanese toward contracts. He believed that these attitudes would change and become more 'Westernised' over time.[4] When asked how the perceived gap between contracting practices and law in the books was to be filled, Kawashima basically saw this as a matter of feudal contracting practices adapting to modern legal values idealised in the codes and given due weight in the courts.

Similar opinions were held by legal scholars such as Toshio Sawada who had conducted extensive fieldwork, exploring the roles played by contract documents and contract law in Japan. His surveys attested to the validity of the hypothesis that rules of positive law are generally neglected in Japanese business practice.[5] He explained this by pointing out that resort to law in contractual matters is generally incompatible with the basic characteristics of the Japanese. Contracts are not viewed as a set of legal claims, but rather as evidence of certain social or personal relationships. The parties are not quite independent since the contractual relationship in Japan is often characterised either by patriarchal benevolence and submissiveness or by the superimposition of personal relations. Just like Kawashima, he concluded that changes were taking place, since Japan was moving towards a more individualistic society, but he argued that a number of traditional Japanese traits still regulate the conduct of business, particularly among businesses conjoined in vertical or horizontal associations.[6]

Kawashima's theory has exerted a great deal of influence both within and outside Japan. Part of the appeal of his suppositions was probably concurrent with the theory of Japan's social uniqueness, which was most popular in both Japan and the West during the 1960s and 1970s.[7] Many legal scholars still rely on his theory as an explanation for current Japanese contracting practices.[8]

However, since the 1980s many of these Japanese legal scholars have become less critical of Japanese contracting practices, which they believe to be distinct from those in the West. This may have been caused partly by the self-assurance which many of them had gained through their country's economic success. Many of them also contrasted a Japanese concept of contract with a 'Western' concept and believed that in Japan the relationship of trust is much more important than the formal contract.

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1 T.Kawashima (1967), *Nihonjin no hōishiki* (The Legal Consciousness of the Japanese). Partially translated by Charles S.Stevens as 'Contract Consciousness of the Japanese' (1974), *Law in Japan,* Vol. 7, p. 1–21.

2 Ibid., p. 15–18.

3 Ibid., p. 21.

4 Ibid., p. 20.

5 Toshio Sawada (1968), *Subsequent Conduct and Supervening Events: A Study of Two Selected Problems in Contract Jurisprudence,* p. 162.

6 Ibid.,p. 179–182, 225.

7 For a strong rebuttal of this so-called *'Nihon jinron'* (Theories of Japanese uniqueness developed for and by the Japanese) see P. Dale (1990), *The Myth of Japanese Uniqueness.*

One other influential legal scholar, Eiichi Hoshino, also pointed to the gap between Japanese contracting practices and law in the books, but was less critical of contemporary Japanese contracting practices than Kawashima. He suggested a different vision of legal values that might recognise and also validate such practices. For example, he argued that the Japanese concept of the contract has influenced contract law itself.[9] This is illustrated by case law where courts use such expressions as 'the parties' trust relationship', which may be influenced by this concept. However, at the same time he stressed the importance of comparing Japanese case law with the case law in other countries before drawing any definite conclusions.[10]

One legal scholar pointed to the gap between a typical Japanese notion of rights and obligations based on Japanese trade norms and the notion of rights and obligations based on contract law as set out in the Codes. This gap often becomes clear when continuing contracts such as distribution agreements are terminated for opportunistic reasons by the supplier. Even though the distributor as the weaker party may believe that the supplier has caused a breakdown in the parties' trust relationship by terminating, he usually simply absorbs the consequent loss without initiating any legal proceedings. When disputes arise as to how to compensate the distributor for his loss the latter can only rely on contractual rights with which he is not familiar. He has usually not anticipated any termination and has not deliberated upon any countermeasures in case the supplier terminates the agreement. Even if parties have agreed on a fixed contractual period they do not attach much weight to such as period. The termination usually does not correspond to the expiry of the period.[11]

An increasing number of practising lawyers also started to focus on distinctive Japanese contracting practices. They argued that strict insistence on contractual rights is much less accepted than in the West, since it may only damage the parties' trust relationship.[12] Some of them referred to international disputes between Japanese and foreign companies in order to describe the differences between Japanese and Western attitudes toward contracts. For example, they referred to a famous dispute between Japanese sugar refinery companies and an Australian company in the 1970s to point out that the Japanese approach toward contracts is more flexible than the Western approach.[13]

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8 This may be caused by the fact that many of these scholars tended to read him a-historically. Kawashima limited himself to traditional contracting practices, which would become 'Westernised' over time.

9 Eiichi Hoshino (1986), *Nihon ni okeru keiyakuhō no hensen* (The Transition of Contract in Japan) in: *Minpō Ronshū* (Collected Essays on Civil Law, Vol. VI), p. 302; See also E.Hoshino (1979), L'évolution du Droit des Contrats au Japon (The Evolution of Contract Law in Japan), Journées de la Société de la Législation Compare, p. 444.

10 See Eiichi Hoshino (1986), *Keiyaku shisō keiyakuhō no rekishi to hikakuhō* (Contract Thought, The History of Contract Law and Comparative Law) in: *Minpō Ronshū* VI, p. 264–265.

11 Noboru Kashiwagi (1992), *'Nihon no torihiki to keiyakuhō: Kyōdō kenkyū—keizokuteki torihiki o kangaeru'* (Japanese Trade and Contract Law: Joint Research—Continuing Trade Considered), 500 *New Business Law* 22–23.

Recently, many European lawyers with experience in Japan have also focused their attention on the distinctive attitudes of the Japanese toward contracts, which are mainly attributable to cultural factors.

### *EU- Japan Legal Symposium on Contract*

During the recent EU-Japan legal symposium in 1996 on contract, which was organised by the Kyoto Comparative Law Centre, most of the attention was directed towards continuing commercial contracts and actual practice. Many of the European lawyers with experience in Japan, who participated in this symposium, referred to the differences in contracting practices between Japan and the EU countries, which some of them attributed to being mainly due to cultural factors. They emphasised the Japanese tendency to use brief contracts and their strong reliance on mutual trust and personal relationships instead of the formal contract.[14]

Some of these practitioners reasoned that when problems occur in transnational dealings between Japanese and European companies the distinctive Japanese attitudes toward contracts become evident. They often referred to disputes which were caused by unilateral terminations of a continuing commercial contract.[15] Based on his own experience in Japan, one lawyer concluded that the termination of continuing contracts shows the obvious interference of cultural factors in dispute resolution matters. However, he also emphasised that different cultures within the EU also result in different approaches to contractual issues. In his opinion, the essential difference with Japan is that when Japanese firms deal with foreign parties, which do business in Japan, the Japanese parties systematically stress the cultural issue as the essential element to take into account for the satisfactory outcome of the relationship.[16]

One practitioner argued that traditionally the Japanese reduce any risks by placing much emphasis on getting to know the party with whom they are dealing and relying on good faith. This seems to be of greater importance than the protection provided by the terms of the contract or the underlying legal system. This may in part explain why domestic contracts are brief and why there are so few lawyers in Japan practising domestic commercial law.

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12 See Saiji Tanaka and Mikio Ueno (1993), *Keiyaku bunshō tokuhon* (Contract Document Reader), p. 14.

13 The dispute started when the Japanese side incurred heavy losses after the international market price of

sugar had suddenly dropped well below the fixed price originally agreed upon. The Japanese companies demanded a price adjustment and refused to continue the purchase of sugar for this fixed price. They contended that the agreement should be reviewed every year. In contrast, the Australian company held that the Japanese companies should purchase the sugar for the fixed price originally agreed upon during the remainder of the five-year contractual period. See Yoshiharu Ishida (1979), *'Nihon to ōbei no keiyaku ni tsuite no kangaekata'* (The Way of Thinking concerning Contracts in Japan and the West), 7 *Kokusai Shōji Hōmu* 444–449.

Furthermore, it may explain why there is so little commercial litigation or arbitration in Japan.

He suggested that current attitudes toward contracts owe much to the *keiretsu* system in which the contracting parties all feel part of one group and therefore the group interest dominates. Furthermore, another factor may be that the smaller non-affiliated companies often supply only one or two other companies with their products or services.

However, he stressed that trading only within groups is less widespread than before and the possibilities of a contractual dispute seem greater than previously. The reliance of contracting parties on a mixture of trust and implicit understanding of their rights and obligations in any given circumstances seem less strong than previously. In domestic contractual relationships gradually more reliance needs to be placed on the legal system. These signs of changes in the attitudes toward contracts are, according to him, caused by similar influences to those which have affected Europe and the US. He was, however, careful not to focus too much on cultural differences since they exist as much between the individual EU member states as between those countries and Japan.[17]

## 3
## CRITICISM OF THE EMPHASIS ON CULTURAL FACTORS

Since the 1970s further empirical research has been conducted in which Kawashima's propositions were checked. Based on the results of this research, many legal scholars started to raise doubts about the supposed differences in contracting practices between Japan and the West. They argued that the disparity between contract rules developed by lawyers and contract practice developed by business is not only characteristic of Japan but also of many other legal systems. Furthermore, through detailed studies of different categories of contracting parties and specific contract types, they discovered more similarities with other countries than had previously been widely assumed.

An increasing number of scholars contended that even if there are distinctive Japanese contracting practices, these have too often been merely attributed to cultural factors and a supposedly 'typical' Japanese concept of the contract. They argued that for a comparative

14 See Guntram Rahn, *'Cultural Differences and Doing Business in Japan'*, Bertil Villard, *'Conclusion of Contracts, Contractual Remedies and Dispute Settlement: A European Practitioners View'*; David Baker, *'Euro-Japan Legal Dialogue Practical Contract Issues'*; Marie Louise Flach de Neergaard, *'Impediments to Negotiation and Fulfilment of Contracts in Japan'* Unpublished papers presented at the EU-Japan Legal Dialogue: Contract, (Kyoto, November 21–22 1996). Currently on the Internet site: http://www.kclc.or.jp/EUdialogue/EU.htm

15 One example may be the apology which is frequently given by the Japanese companies after complaints about their product from the other party. This is not easily provided by Western companies. See Cees Vellekoop, *'Bridging the Gap between Different Legal Business Cultures'*; Laurent Dubois, *'Contracting in Japan: Between Trust and Suspicion'*, unpublished papers presented during the EUJapan Legal Dialogue: Contract, (Kyoto, November 21–22,1996).

16 See the unpublished paper presented by Laurent Dubois during the EU-Japan Legal Dialogue; Contract. (Kyoto, November 21–22 1996).

research of contracting practices it is important to also study the impact of other factors relevant to contract norms within each society.

For example, the results of a survey on the use and non-use of contract law in Japan and the US caused an American legal scholar to avoid immediately ascribing distinctive features in the two systems to cultural factors. He focused on the identity of the parties whose perceptions of contracts are being described and pointed out that many legal scholars have directed their attention towards the attitudes of different groups in Japan and the US. These are Japanese business people, on the one hand, and American lawyers on the other. Such comparisons between the two countries can be very misleading. He concludes that in order to gain an accurate insight into attitudes and practices it is necessary to confine investigations to particular lines of business or types of transaction.[18]

One Japanese legal scholar discovered in his survey that written contracts are used much more frequently in Japan than was previously assumed and this is due to the increasing number of laws which have directly or indirectly required parties to make use of contracts.[19] He contended that the type of contract used in Japan does not necessarily depend on the cultural context but rather on such factors as the nature of the trading relationship and the applicable legal rules. Based on his research into the use of contracts within the automobile industry in both the US and Japan, he discovered that contracts in the US are more comprehensive than in Japan, but explained this as being partly due to the background of these industries. For example, in the contracts between Japanese automobile manufacturers and their dealers the provisions on termination are very short because of the fact that litigation initiated by dealers is non-existent. Therefore, the Japanese manufacturer does not spend much time in employing legal specialists to draft any precautionary contract terms.[20]

One American legal scholar has conducted research in the Japanese banking industry, where he focused on the role of legal rules when the trade relationship is terminated. He discovered that those who defect often enforce their legal rights. Furthermore, banks deliberately use short contractual terms, keeping the terms of their loans short. This is done in order to retain the right to refuse to renew the loan and thereby to be able to reduce the default risks from their borrower's opportunistic strategies. He argued that law matters because there is always a risk of defection even in markets where parties have continuing relationships and invest in their reputation.[21]

Recently, strong doubts about the existence of a 'unique' Japanese concept of the contract, explained by Japanese culture, have been raised by the Australian academic Veronica Taylor. First, she argues that sweeping comparisons of Japanese contracting with law and practice in 'the West' have outlived their use and comparative studies which analyse the market characteristics of different contract types in Japan are needed. Furthermore, she contends that static representations of Japanese contract norms as if the law is largely

17 David Baker, *'Euro-Japan Legal Dialogue Practical Contract Issues'*. Unpublished paper presented during the EU-Japan Legal Dialogue: Contract (Kyoto, November 21–22 1996).

irrelevant to Japanese contracts, that the Japanese favour unwritten agreements and do not feel bound by their contractual commitments are false and misleading.[22] She states that readers of Kawashima have assumed that positive law and judicial or scholarly analysis have little impact on contract practice in Japan, but such conclusions are incorrect since the nature of the legal system influences contract practice even when legal regulations are disregarded and formal requirements breached.[23] She argues that a dynamic combination of commercial customs, legislative reform and case law fashion contract law and contract practice in Japan. The Civil Code and Commercial Code influence the structure and performance of contracts in Japan. However, law in the books is not static and over the years these Codes have been amended by judicial and statutory intervention. One example is the strong indirect impact of the Anti-monopoly Act. She further argues that positive law and the impact of new types of contracts such as distribution agreements on classical contract doctrine are significant components of Japanese contracting.[24]

Finally, it is important to refer to the Japanese legal scholar, Takashi Uchida, who also raised doubts about Kawashima's strong focus on dualism in Japanese contract law. He argues that this dualism is not unique to Japan, but exists in many other countries as well.[25] For example, the 'avoidance of contract', which was believed to be typically Japanese, can also be found in the US.

Recently, a group of Japanese scholars led by Uchida and some American legal scholars have carried out comparative empirical research into domestic continuing commercial contracts in various industries in both the US and Japan. The findings which were based on their extensive surveys and interviews in Japan and the US confirm the conclusions of prior research that contracting practices within continuing commercial relationships in both countries have a great deal in common.[26] This also applied to terminating patterns. They discovered that in both countries legal rules are considered less important than economic factors as long as the terminating party does not want to resort to the courts.[27] In general, their findings made them cautious about focusing too much on distinct Japanese contracting practices, which can be attributed to cultural factors. It is also interesting to refer to the

18 W.Gray (1983), 'The Use and Non-use of Contract Law in Japan: A Preliminary Study', in: *Law and Society in Contemporary Japan,* J.O.Haley (ed), p. 243–262.

19 See T.Ōta (1989), *'Kōkan katei ni okeru keiyaku no yakuwari. Nichibei no hikaku o chūshin ni shite'* (The Role of Contract during the Process of Exchange. An Emphasis on the Comparison between the US and Japan). in: K.Fujikura & N.Nagao (eds.) *Kokusai masatsu sono hōbunkateki kankei* (International Friction and its Legal Culture Backdrop), p. 227–229.

20 Ibid., p. 243–260.

21 See also J.M.Ramseyer (1991), 'Legal Rules in Repeated Deals: Banking in the Shadow of Defection in Japan', 20 *Journal of Legal Studies* 91–117.

22 See Veronica Taylor (1993), 'Continuing Transactions and Persistent Myths: Contracts in Contempo-rary Japan', 19 *Melbourne University Law Review* 353.

23 Ibid., p. 361.

24 Ibid., p. 354.

fact that the findings of the surveys and interviews conducted within Japan indicated that there exists a great variety among the different Japanese industries as regards the attitudes toward contracts.[28]

It is important to notice that Uchida takes care to avoid a 'Japan vs. the West' type of mental framework. He argues that differences between Japan and the US have often been misleadingly translated as differences with the 'West'. For example, comparisons with contracting practices in European countries are very important.[29]

Finally, Uchida believes that it is necessary to distinguish between trade customs, which are also common in other countries, and those that are uniquely Japanese. According to Uchida recent studies by Japanese economists have found that the trade customs in Japanese vertical trade relationships, which are important with respect to contract law, took shape during the period of high economic growth after World War II. Therefore, it would be a mistake to attribute the gap between trade customs and contract law to a traditional Japanese concept of the contract, which already existed before the introduction of Western law.[30]

## 4
## MY OWN CONCLUSION

Partly on the basis of my own research into Japanese contract law and anti-trust law, my field research within the Japanese distribution system for luxury cosmetics and the comparison with Dutch law and practice, I tend to agree more with the legal scholars who do not focus their attention too much on 'distinctive' Japanese contracting practices. Furthermore, in my opinion one must take into account the strong impact of factors other than cultural ones. I share the doubts about a typical Japanese concept of the contract and disagree with the use of Kawashima's theory for any static representations of Japanese contracting, usually caused by assuming the existence of a unique cultural identity.

### *Japanese Contract Law*

After studying Japanese case law and legal comments in relation to the termination of distribution agreements, I found that in most cases when applying the principle of good faith Japanese courts pay little attention to the contents of the underlying contractual terms

25 As mentioned in Chapter 2, Takashi Uchida believes that the dualism of contract norms supposed in the relational contract theory of MacNeil may be a suitable theoretical mcxiel for the dualism in Japan between formal and 'living' law. See T.Uchida (1990), *Keiyaku no saisei* (The Rebirth of Contract).

26 The results of this research were published in a series of six articles in *New Business Law* from 1997 to 1998: No. 627 p. 6–18; No. 629 p. 47–52; No. 630, p. 52–60; No. 631, p. 6–15; No. 632, p. 55–63; No. 641, p. 15–20.

27 See J.O.Haley (1998), *'Nichibei in okeru kankeiteki keiyaku—chigai wa aru no ka- Kyōdō kenkyū keizokuteki torihiki o kangaeru no Nichibei hikaku'* (Relational Contracts in Japan and the US—Are there any Differences? Joint Research: Continuing Trade in Japan and the US Compared), (translated by T.Uchida), 641 *New Business Law* 16.

when considering all the relevant circumstances for their decisions. On a number of occasions the Japanese courts did not consider the distinction between contracts of a fixed period and an unfixed period to be very important. Even when compared to Dutch case law, which is of a comparable nature, it seems that Japanese judges pay less attention to underlying formal contractual terms. Here we notice a marked difference in judicial reasoning between Japanese and Dutch judges.

Japanese judges seem to enjoy greater flexibility in deciding disputes when they apply concepts such as 'unavoidable reasons' and a 'breakdown of the parties' trust relationship'. While relying on their competence to interpret contracts in these termination disputes they have often interpreted the contractual terms to mean something different from what the parties had clearly spelled out in the contract.

These factors seem to point to the minor importance of contracts within Japan as posited by Kawashima and others. This would imply that Japanese courts would more or less recognise Japanese contracting practices, where contracts and contract law as stipulated in the Codes may be irrelevant to the parties.[31] Here it seems that indeed generally speaking in Japan the principle of private autonomy is less influential.

However, in my opinion, it would be wrong to take this as evidence to confirm the Kawashima thesis. On closer examination, differences between Japanese and Dutch case law are not wide enough to warrant such an extended interpretation. Dutch judges may be less ready to reinterpret the meaning of clear and agreedupon terms at their own discretion, and prefer rather to intervene by invalidating terms based on the 'restrictive' function of good faith, but the method of 'interpreting' the contract in a reasonable way is not unknown in Dutch judicial practice. While applying the good faith principle the Dutch courts also focus on subjective circumstances within a similar civil law tradition. The Dutch courts also frequently interfere with the contractual terms and reach similar conclusions as the Japanese courts.[32]

Still, the widespread use of the concept of the 'breakdown of the parties' trust relationship' in Japanese case law and legal literature may be a sign that some difference exists between the Japanese and Dutch business communities with respect to the degree of trust within the commercial relationship between the suppliers and the distributors.

This explains the strong 'bias towards renewal', which has been confirmed in Japan by some influential court decisions.[33] Many legal scholars who contributed to the discussion on Japanese attitudes toward contracts have also referred to the great importance in Japan

28 In 1994, during the first year of this empirical research within Japan I participated in several interviews which were conducted by Uchida and his group.

29 T.Uchida (1993), *Zadankai* (Round Table Discussion) '*Gendai keiyakuhō no aratana tenkai to ippan jōkō*' (New Developments in Contemporary Contract Law and General Clauses), 515 *New Business Law* 14–15.

30 Ibid.,p. 15.

31 See E.Hoshino (1986), o. c., p. 264–265.

of the parties' trust relationship. This has also been confirmed by empirical research within Japan.[34]

However, it is important to note that recently in relation to termination disputes the Japanese courts have tended to place more emphasis on the principles of classical contract law, such as the freedom of contract. An increasing number of decisions have attached more weight to the underlying formal contractual terms. This may indicate a growing tendency among Japanese contracting parties to attach more value to contracts. Therefore, the use of brief contracts and a stronger reliance on trust are not due to timeless cultural idiosyncrasy. Many factors such as the current poor economic climate and internationalisation may have reduced the reliance upon unwritten social codes and mutual trust. They have probably had some influence upon some recent court decisions concerning the termination of distribution agreements, which were more legalistic than previously.

To put Japanese case law and its function into a proper perspective it is important to realise that although there exists a body of case law in which small distributors are protected, litigated termination disputes in Japan are still limited in number. From the start of the 20th century until 1994 there were only approximately 60 litigated termination disputes where the manufacturer/suppliers had cancelled their distribution agreements with the distributor.[35] Within the Netherlands, which compared to its neighbouring countries has a limited number of litigated disputes, this number is probably still higher when taking into consideration that a great deal of such litigated termination disputes are not reported in the Netherlands.[36] Given the comparatively small size of the Netherlands in relation to Japan it is obvious that in Japan distributors initiate legal proceedings less readily.

One could interpret this difference as confirmation of the existence of a distinct concept of the contract by the Japanese who do not insist on contractual rights when the distribution agreement is terminated. However, in my view this difference is mainly due to the fact that Japanese civil courts are less easily accessible than the Dutch courts. Barriers to litigation also exist in the Netherlands but less so than in the Japanese legal system. Japanese distributors have less to gain from state intervention. The smaller number of judges and trial lawyers, filing fees, bond-posting requirements and other disincentives such as the lack of a summary injunction procedure together increase the costs of litigation and effectively restrict access.

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32 See the interesting discussion between the former Dutch judge J.H.Nieuwenhuis, T.Uchida and N.Segawa during the symposium 'Dutch and Japanese Laws Compared' (Tokyo, November 9–10, 1992) published in 1993 by the International Centre for Comparative Law and Politics, p. 141– 145. J.H.Nieuwenhuis referred to a similar meaning and function of the good faith principle in both countries and stated that Dutch courts would easily reach the same decision as the Japanese High Court in the famous 'Hokkaidō Tractor Case'.

33 The results of the extensive survey into trading practices within Japan, headed by T.Uchida, showed that the Japanese companies usually trade for a long period in which short-term contracts are renewed repeatedly. See Shūgō Kitayama (1997), *'Keizokuteki torihiki ni kansuru kokunai ank to chōsa no kekka'* (The Results of the Domestic Survey on Continuing Trade) 627 *New Business Law* 13–17.

Compared to the Netherlands there are fewer incentives for the distributors to take legal action. This may be the main reason for the fact that distributors rarely insist on their contractual rights and claim performance of the contract or damages before the courts.

### *Case Studies within the Japanese Distribution System for Luxury Cosmetics*

My tendency to raise doubts about distinctive Japanese attitudes toward contracts is primarily based on my field research within the Japanese distribution system for luxury cosmetics and the comparison with a similar distribution system in the Netherlands. I discovered that written contracts and contract law as set out in the Civil and Commercial Codes can be very important for the leading manufacturers when terminating their contracts.

The standard-form distribution agreements, which are used by the leading manufacturers of luxury cosmetics, are an important tool to ensure that the distribution system remains closed and tight. The case studies have shown that these contracts are strongly relied upon when the attempted extra-judicial sanctions are no longer effective to bring discounters/ distributors more into line with their sales policies.

In most cases the manufacturers based the termination on the provision which entitles them to terminate the contract intermediately with at least 30 days' notice. Some manufactures decided not to renew the distribution agreements after the expiry of the contract period. This means that manufacturers strongly relied on general principles of contract law such as the principle of freedom of contract. Only when they were required to give a good reason for the termination before the courts did they point to several duties and prohibitions within the contract, which were allegedly breached by the discounters.

The importance of their standard-form contracts is also illustrated by the fact that the majority of manufacturers decided to amend existing contracts or to draft new contracts for newly established brands. Within these new contracts the duty to sell face-to-face was strengthened and made more explicit. This would make it easier to terminate if distributors would not abide by this sales method. The manufacturers must have realised that some of

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34 The results of the same survey showed that most Japanese companies believe that the relationship of trust plays the most important role in resolving disputes. See Hiroyasu Nakata (1997), *'Keiyaku to kankei—keizokuteki torihiki no chōsa kara'* (Contracts and Relations—From the Survey on Continuing Trade), 631 *New Business Law* 11–12. Furthermore, based on previous empirical research it appears that Japanese companies often refer to the relationship of trust that they have established with their trading partners as one of the most important reasons for continuing business with them. See H.Nakata (1994), *Keizoku baibai no kaishō* (The Termination of Continuing Sales), p. 45.

35 See H.Nakata (1994), Ibid., p. 57–105.

36 The number of reported cases where manufacturers had terminated contracts with distributors described by Van de Paverd is already approximately 30. See C.A.M.van de Paverd (1999), *De Opzegging van Distributieovereenkomsten* (The Termination of Distribution Agreements), (PhD Thesis, Amsterdam), p. 347–350.

these contractual provisions had been too vague, which had also contributed to the emergence of the termination disputes with the discounters.

Furthermore, their completely new contracts were only concluded with retailers which followed their sales policies. In this way they could also omit the discounters without having to terminate contracts.

The decision to amend existing contracts and to draft new ones was triggered by the challenges to their distribution system from the association of discounters which has led to a number of court decisions and a great deal of publicity within Japan. A similar phenomenon can be seen in many franchise distribution systems where vague and incomplete contracts have recently been made more explicit by the franchisers due to an increasing number of disputes between them and the franchisees.[37]

These case studies demonstrate that the Anti-monopoly Act in particular can have a strong indirect impact on contracting and terminating behaviour by the manufacturers of luxury cosmetics. They were very concerned as to whether the terminations, and the contractual terms on which these were justified, might have violated the Act. Many manufacturers became wary about terminating contracts with discounters. Furthermore, Anti-monopoly Act observance manuals were drafted for internal use and Shiseido even established a legal department partly because of its running disputes with the association of discounters.

On the other hand, the group of discounters had a strong weapon by invoking anti-trust law. In the beginning this was mainly limited to complaints with the FTC, but over the years, invoking this law before the civil courts became more influential. They realised that when taking on such leading manufacturers it is insufficient to only invoke the principle of good faith and demand the specific performance of the contract. The threat of invoking anti-trust law exerted far more influence upon the leading manufacturers.

Accordingly, both manufacturers and distributors became increasingly aware of any possible infringements of the Anti-monopoly Act. It is no exaggeration to say that anti-trust law became the most influential factor in these termination disputes. As shown by the case studies many manufacturers fear the disclosure of a possible violation of the Act because it results in negative publicity. In view of the fact that anti-trust law issues in relation to the termination of distribution agreements also increasingly occur in other industries, the conclusion that the Act exerts a great impact on contracting and terminating attitudes is justified. Previous discussions on Japanese attitudes toward contracts have rarely pointed to this important aspect.

Furthermore, these cases also underlined that there are many formal barriers for distributors when deciding to initiate legal proceedings against their suppliers. They demonstrated that initiatives by distributors to create legal precedents by litigation face numerous difficulties. It requires a great deal of perseverance when taking recourse to the civil courts. Taking on large companies within the Netherlands is also not easy but in Japan it seems even more difficult.

The cases highlighted in chapter 4 where distributors took on the manufacturers until the very end are very exceptional. The lawyer who represented the discounters, Jirō

Yamane, and the president of Fujiki, Ken Fujisawa, attached much importance to the maintenance of moral values rather than to thoughts of economic profit. Their disputes by no means represent the mainstream of distributors in Japan.

### *Comparison with the Dutch Distribution System for Luxury Cosmetics*

My comparison with the role of law in the Dutch distribution system for luxury cosmetics has furthermore shown that the standard-from contracts which are used by the leading, usually French, manufacturers of luxury cosmetics are longer and more detailed than those in Japan. However, the provisions on termination do not differ very much. In my opinion this difference cannot be merely explained by cultural factors. It may partly be due to the more detailed rules of EU anti-trust law in relation to selective distribution systems as laid down in numerous decisions of the Commission and the Community Courts.

Another reason for more detailed contracts may be that the large French manufacturers use similar standard-form contracts in many different EU countries. This enhances the need for more detailed contracts.

As regards the terminating attitudes of the manufacturers in both countries I do not believe that these attitudes differ very much. There are no indications that the Dutch exclusive importers or subsidiaries, on the one hand, and the Dutch selected distributors on the other, are more legalistic than the Japanese manufacturers and distributors, or that contracts matter more than in Japan when it comes to the termination of contracts.

The suppliers of luxury cosmetics in the Netherlands often terminated contracts with their distributors but usually did so amicably. They have limited the number of their outlets but this has rarely led to litigation. Only when contracts were cancelled with immediate effect did distributors initiate legal proceedings. However, such cases are very limited. Manufacturers do not want to risk litigation and the development of legal precedents which may turn against them and therefore they agree to terminate contracts amicably. As in Japan the relationships are usually wound down gradually.

However, although Japanese manufacturers also fear the possible development of legal precedents created by the FTC or the civil courts which could oblige them to change their distribution network, this fear seems to be stronger in the Netherlands for the simple reason that there are less formal barriers to any legal proceedings by the distributors. In contrast, the Japanese manufacturers seem to be more afraid of negative publicity.

In Japan civil courts have a less strong role in enforcing the Act. For example, the lawyer, Yamane, primarily based his hopes on a complaint with the FTC and only as a last resort went to the civil courts. Furthermore, the stronger ambiguity in Japan about the exact

37 See M.Sugawara, J.Imai and K.Hosoda (1998), *'Furanchaizu hikari to yami'* (Franchise, Light and Darkness) in: *Nikkei Business* 23 February 1998, p. 23–24; H.Tanaka and K.Fukuzawa (1998), *'Furanchaizu no jigoku'* (The Franchise Hell) in: *Shūkan Daiyamondo* 20 June 1998, p. 24–45.

relationship between anti-trust law, on the one hand, and the Civil Code and the civil procedural rules on the other may also have a great deal of impact.

To sum up, it can be concluded that compared to the Netherlands there are not so many differences in contracting practices. In my opinion existing differences such as the smaller number of litigated termination disputes and the longer and more detailed distribution agreements within the cosmetics industry should be mainly attributed to a difference in the enforcement mechanism within the legal system. It is very important to point out that the civil courts in Japan are less easily accessible. Therefore, the contrasts that I have identified are really due to differences between the two legal systems themselves, rather than to different concepts of contract.

However, the strong emphasis on the parties' trust relationship may be an important distinctive feature in Japan, indicating that many companies still rely more on this relationship of trust than on the formal contractual terms. Further research into this concept is needed.

The Civil Code principles such as the principle of freedom of contract and the Anti-monopoly Act may have a stronger impact in Japan on contracting attitudes than many legal scholars seem to assume, because these scholars still tend to focus on a distinct Japanese concept of contract and argue that law is largely irrelevant for Japanese contracts. This can in part be explained by a lack of knowledge of contracting practices in Western countries, which turn out to be less different than previously assumed. Sweeping comparisons with 'the West' should be avoided and more comparative research into similar types of transactions in Japan and Europe is necessary.

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# Curriculum vitae

Willem Visser 't Hooft is an expert on Japanese law. For his PhD thesis he was affiliated with the University of Tokyo and the University of Leiden. Currently he lectures at Dutch Universities on Japanese law.