

Introduction

We have received a number of inquiries about the coronavirus disease 2019 (COVID-19) and what organizations should be doing to mitigate the impact of the virus on their staff, supply chains, operations and other aspects of their business in Japan.

We have prepared this bulletin as an overview of some key legal issues for businesses operating in Japan or dealing with Japanese counterparties to consider, to offer some practical steps for businesses to take. These include contract and commercial matters (*force majeure*, material adverse change and dealings with subcontractors), employment matters (working from home, forced leave and changes in working hours) and company matters (developments with respect to delays in timely disclosure and convening virtual shareholder meetings that may affect investors in Japanese companies).

We hope this bulletin will be helpful to you as you navigate your way in doing business in Japan during these unprecedented circumstances.¹

Contract and Commercial Matters

Force Majeure

Force majeure provisions in contracts operate to relieve parties of their obligations under circumstances outside of their control, such as war, natural disasters and the like. They are commonly included with other “boilerplate” provisions in commercial and other transactional agreements.

Like any other contract provision, the effect of a particular *force majeure* clause will depend on its specific language and on the underlying facts at hand, i.e., not all *force majeure* provisions are the same. Where a party is prevented from performing, or where there is a risk that a contract counterparty might attempt to avoid performance, good practice requires a careful analysis of the actual language of any applicable *force majeure* provisions to assess potential legal claims.

In contracts currently under negotiation, it will be important to ensure that any relevant *force majeure* provisions are carefully drafted, to properly allocate the risk related to the current COVID-19 situation.

It is noteworthy that under Japanese law, a party to a contract *may* still be excused from performing if prevented by external events even if an express *force majeure* provision is not included in the contract. In this regard, contractual performance can sometimes be excused on the basis of *force majeure* if performance is prevented by an event that is not controllable by a natural person, and is instead the result of external factors that could not be avoided through the exercise of reasonable care. Whether this Japanese law doctrine could apply, even in the absence of an express *force majeure* provision, will typically require a careful consideration of the parties’ respective positions and the circumstances of the agreement at hand.

Finally, a major revision to Japan’s Civil Code is scheduled to take effect from April 1, 2020. At present, if a party is excused from performance on the basis of a *force majeure* event, the counterparty may not terminate the contract.² Under the amended provisions to the Civil Code, the counterparty will have the right to terminate the contract.³

Material Adverse Change

In M&A transactions, purchase agreements frequently include material adverse change (MAC) (also referred to as material adverse effect (MAE)) clauses, pursuant to which a buyer may walk away from a transaction after signing, but before closing, if a MAC has occurred. Such MAC clauses might only be triggered by very specific events, or they might be broader in scope. Given the risk that COVID-19 could potentially affect all aspects of a target business, potential buyers should focus on how such risks are allocated by the MAC clause. In addition, for any agreements already signed, it will be necessary to evaluate whether the MAC clause is or could be triggered. Such analysis would be fact-specific and depend on the MAC clause wording. Note that under some purchase agreements, the effects of COVID-19 might be excluded as a change in the general economic market, political conditions, natural disasters or other event that does not affect the business disproportionately compared to other companies in its industry generally.

Buyers who are concerned about the potential impact of COVID-19 on the target business/assets should consider negotiating for a purchase price adjustment provision, which would help to allocate short-term risks related to COVID-19.

¹ Situations and circumstances created by the COVID-19 pandemic are changing rapidly, often on a daily basis (for example, the unprecedented step of postponing the 2020 Tokyo Olympics). Our Tokyo office is committed to supporting our clients and friends in these unsettling times and plans to provide ongoing updates through additional bulletins. Of course, the Tokyo office, as well as any and all other parts of the firm, stands ready to assist you and your company on specific legal issues arising from this crisis.

² Japan’s pre-reform Civil Code, Article 543.

³ Japan’s post-reform Civil Code, Articles 541-543.

Dealings With Subcontractors

In Japan, a unique law referred to as the Subcontract Act⁴ exists to maintain the fairness of transactions between a contracting principal and its subcontractors, protect the interests of subcontractors and restrict misconduct such as refusal of receipt of performance, payment delay and reductions in payments, or other abuses against subcontractors.

On March 10, 2020, Japan's Ministry of Economy, Trade and Industry (METI) issued a series of administrative "requests" targeting companies engaged in transactions with mid- and small-sized subcontractors that may be affected by COVID-19, as follows:⁵

First, contracting principals should be aware that subcontractors may be delayed in meeting delivery dates due to shortages in materials and/or labor due to the effects of COVID-19. METI indicated that in such situations, contracting principals should be flexible in their responses to delayed delivery dates and seek to continue to conduct business with such subcontractors without seeking compensation for losses.

Second, contracting principals should pay their subcontractors the subcontract price, plus additional costs arising as a result of the effect of COVID-19 on the price of raw materials and/or the costs of overtime and the like caused by shortened delivery lead times.

Third, contracting principals are to exercise flexibility and discuss payment dates and payment methods again irrespective of the prescribed payment terms, considering that subcontractors may be experiencing cash flow difficulties due to a decrease in orders.

Fourth, if a contracting principal cancels orders or changes order quantities, specifications or other terms owing to COVID-19, the contracting principal is to consult with its subcontractors and pay for the cost of work in progress to ensure that no losses are incurred.

How these recent "requests" by METI will be followed, in practice, has yet to be seen. Further, while contravention of any of these suggestions of METI would not technically amount to a breach of law, it might be considered to constitute a violation of the Subcontract Act, although it is also currently unclear what METI will consider the ramifications of such a violation to be.

Employment Matters

Work From Home

COVID-19 has caused many employers in Japan to implement work-from-home arrangements. If a company's work rules provide for the employer's right to do so, an employer can require its employees to work from home. If not, the work rules may need to be amended to enable the employer to require working from home.

It is crucial for an employer in Japan to bear in mind that even when employees are working from home, Japan's laws applicable to labor and employment generally, including the Labor Standards Act, continue to apply. Employers should ensure, for example, that employees continue to abide by laws and work rules/handbooks relating to working hours, working on holidays or working late at night. It is important that employers convey these expectations clearly to employees.

Under the Labor Standards Act, employers are required to introduce work rules providing for allocation of costs of the items necessary for working from home, such as laptops, cellphones and WiFi, before implementing working from home.⁶ Laptops, cellphones and other devices are generally supplied by the employer. Because it can be difficult to distinguish between the costs for cellphone and WiFi telecommunications services used by employees working from home from their personal use, a number of employers pay for a fixed amount of an employee's communication costs.⁷

Forced Leave

In Japan, paid and unpaid leave is highly regulated, including when an employer may require an employee take leave from work. Depending on the circumstances, an employer may owe compensation to employees, depending on the circumstances, if, in response to COVID-19, the employer requires employees to take time off from work.

Under Japan's Labor Standards Act, workers who are forced to "take leave" for "reasons attributable to employers" are entitled to receive 60% or more of their applicable average wage during the leave period.⁸ The Japanese Supreme Court has broadly construed the term "reasons attributable to employers."

It is likely in most cases that the placement of employees on leave by an employer for COVID-19-related reasons, including prevention of further infections from COVID-19, are likely to be considered "reasons attributable to the employer," and hence require that the employer compensate its employees.

Conversely, the placement on leave of an employee who has actually been infected with COVID-19, would not likely be considered to be a "reason attributable to the employer," unless the employer itself was somehow found to be responsible for creating the conditions conducive to infection.

4 The Act against Delay in Payment of Subcontract Proceeds, Etc. to Subcontractors.

5 <https://www.meti.go.jp/press/2019/03/20200310003/20200310003-1.pdf> (Japanese language)

6 Japan's Labor Standards Act, Article 89(1)(v).

7 <https://work-holiday.mhlw.go.jp/material/pdf/category7/02.pdf> at p.17 (Q2-7). (Japanese language)

8 Japan's Labor Standards Act, Article 26.

Under Japan's Act on the Protection of Personal Information, employees' infection status likely constitutes "Special care-required personal information,"⁹ which employers are prohibited from collecting without the employees' prior consent (subject to certain limited exemptions).¹⁰ It is likely, however, taking into account the current COVID-19 emergency situation, an employer collecting employee information on infection by COVID-19 will fall within an exemption (as "a special need to enhance public hygiene") and, therefore, employers may be allowed to collect and disclose such information to the Japanese government without the employee's prior consent if it would be difficult to obtain consent.¹¹

Leave for other reasons should be discussed carefully by an employer with its employees after considering applicable legal risks.

Changes in Working Hours

In Japan, overtime hours are generally calculated on a per-day basis. In cases where working hours are prolonged due to labor shortages related to COVID-19, or where working hours are shortened due to reduced business activities, employers may introduce an "Adjustable Working Hour System" (*Henkei Roudou Jikan Sei*) based on a one-year, one-month or one-week calculation period.

Generally, if an employer introduces a one-year calculation system, the employer is prohibited from changing the system for at least one year following implementation. However, the Ministry of Health, Labor and Welfare of Japan (MHLW) has issued guidance that if the one-year calculation system is later deemed extremely inappropriate in light of the impact of COVID-19, the employer may, as an exception, agree with the relevant labor union or a representative of the majority of its employees to terminate the one-year calculation system or enter into a new calculation system.

In Japan, an "Article 36 agreement" (*Saburoku Kyotei*) between the company and the relevant labor union or a representative of the majority of its employees is generally required before a company can cause its employees to work overtime (i.e., so-called "forced overtime"). It is likely that many existing Article 36 agreements do not contain provisions that would directly address the ramifications of something like the current COVID-19 outbreak. Nevertheless, depending on the particular circumstances, the employer might be able to require forced overtime as a "temporary exception." There is no clear precedent of exactly how long an employer may rely on this exception, but it is likely allowable only to the extent the employer suffers a labor shortage caused by COVID-19.

Company Matters

Timely Disclosure Delays

Under the Financial Instruments and Exchange Act, companies with publicly traded securities that are required to submit timely securities reports, internal control reports, quarterly reports and semi-annual reports may be unable to do so due to the impact of COVID-19. For example, audits of certain foreign subsidiaries cannot be conducted at the present time due to COVID-19. With the approval of the Japanese Financial Services Agency, it may be possible to have these submission deadlines extended by showing an unavoidable need for an extension.

Virtual Shareholder Meetings

There is no settled position in Japan regarding the legality of convening virtual shareholder meetings under Japan's Companies Act. This applies to both public and private companies. Nevertheless, taking into account the seriousness of COVID-19, many companies may wish to avoid in-person meetings. In response, METI published guidance regarding virtual shareholder meetings on February 26, 2020,¹² and organizations might consider implementing at least partially virtual shareholder meetings, after obtaining legal advice. If a previously scheduled shareholder meeting needs to be changed for any reason, it is important for the company to ensure that any such changes are effected in accordance with applicable law and charter provisions.

We hope that the foregoing general discussion of rapidly developing legal issues in Japan related to the COVID-19 pandemic is helpful. As always, specific legal advice on a particular situation will depend on the facts and circumstances present. Should we be able to assist with any such situations, please let us know.

9 Japan's Act on the Protection of Personal Information, Article 2(3).

10 Japan's Act on the Protection of Personal Information, Article 17(2).

11 Japan's Act on the Protection of Personal Information, Article 17(2)(iii).

12 <https://www.meti.go.jp/press/2019/02/20200226001/20200226001-2.pdf> (Japanese language)

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