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LEGAL CHARACTERISTICS OF JAPANESE BUSINESS ASSOCIATIONS.

A COMPARISON BETWEEN SUCH ASSOCIATIONS AND AMERICAN PARTNERSHIPS AND BUSINESS CORPORATIONS.

PART I. JAPANESE BUSINESS ASSOCIATIONS PAST AND PRESENT.

For the purpose of understanding the development and present legal status of the business associations of Japan, one may recognize the existence of four periods:

1. The period before 1868.
2. The period between 1868 and 1893.
3. The period between 1893 and 1898.
4. The period since 1898 and 1899.

The year 1868 marks the abolition of the feudal system and the restoration of the imperial government. The Mikado, who had been a nominal sovereign for seven centuries, deprived the Shogun of his power and subdued all the three hundred petty kingdoms. The year 1893 marks the adoption of the law of association embodied in the First Commercial Code. The years 1898 and 1899 mark the adoption of the New Civil and Commercial Codes, under which the business associations of Japan now operate.

1. THE PERIOD BEFORE 1868.

There were no commercial associations organized under statutory or general law in Japan before the restoration. Under a feudal system, the people of different states could not freely communicate with each other. Neither could they have free commercial intercourse with foreigners. Indeed, practically the only intercourse of this kind was with the Dutch and Chinese merchants in Nagasaki. Business men were generally despised, the aristocratic class being composed solely of warriors. It is quite natural that industry could never be developed under such conditions. All kinds of business being prosecuted on a small scale, it was not necessary to provide for the formation of large commercial associations. Again, all private law was in a very undeveloped state, and the small commercial associations which for lack of a better name we may call partnerships, that did exist, were not subject to fixed rules of law. The people transacted their business with each other according to customs and usages handed down from time immemorial. But these customs were not identical in all parts of the country and were not necessarily enforced by the Courts as is the customary law of America. The judges could decide any case according to their own will. If they did not like the custom they could disregard it.

2. THE PERIOD BETWEEN 1868 AND 1893.

During this period, western civilization was introduced. Everything was changed. Many commercial associations for the mangement of banks and the building and operation of railways sprang into existence. These associations were incorporated by special acts, not passed by the Legislature since no Legislative body existed, but issued by the Government as administrative decrees. The Government, not being subject to any constitutional limitations, had an absolute power to incorporate or dissolve an association. The small associations not organized under any statutory provision which we have called partnerships, still continued

to exist. These, as prior to the restoration, were not subject to any certain rules; indeed it was not until the New Civil Code came into operation in 1898 that any law, properly so called, was made for their guidance.

3. THE PERIOD BETWEEN 1893 AND 1898.

The First Commercial Code of Japan was compiled by a German, named Reusler. The law of commercial associations which constituted a part of the Code came into operation in 1893. In the main the commercial Codes of continental Europe were followed. The Code recognized three kinds of business associations—*Société en nom collectif, Société en commendité* and *Société annonyme.*

A. Société en nom collectif.

This was an association, all the members of which assumed a joint and unlimited liability to the creditors. Thus, as in the English and American partnerships of the common law, its members were not only liable for the capital contributed, but also their individual property was responsible for the debt of the association if its capital had been exhausted. The Société was formed by a written contract between the members. They could set forth anything they liked in this contract, if such a thing was not in violation of law. The purpose of the association, the date of its formation and other things prescribed by law had to be recorded with the court. All the members equally had the right and duty to manage the business of the Société. If there were no representative directors stipulated in the contract of membership the general rule was that each member had the power to represent the société, unless the articles of association confirmed the right of management to particular persons. A member's interest in the association could be transferred with the consent of the other members. In the absence of a special contract between the new member and the company, the incoming member was unlimitedly liable for any debt incurred before he was admitted to the membership.

The association was not dissolved by the retirement of a member. Thus, any member might retire: (1) With the unanimous consent of the other members; (2) through expulsion; (3) when the term of the contract of membership had not been fixed or the contract had provided that it should be binding on him through his life; (4) through an order of the Court issued on the application of the other members; (5) through his death, insanity or bankruptcy.

A retired member was not liable for any debt incurred after his retirement, but for two years he was still responsible for the debts incurred during his membership.

The association was dissolved: (1) If one member only was left; (2) if the purpose for which it was organized became impossible; (3) if the term for which the company had been organized expired or any event occurred which had been designated in the original contract as causing a dissolution; (4) if all the members gave their consent to the dissolution; (5) if the association became bankrupt; (6) if the Court issued a decree of dissolution. After the winding up of the association, the members were required to preserve the books and accounts of the company for ten years, but their unlimited liability for the debts ceased five years after the dissolution.

B. Société en commendité.

This was an association composed of non-active members and directors. The members were only liable for the money or property contributed, unless they inserted a special provision in the contract of association. Thus, if one or more of the members chose to assume an unlimited liability, they might make a special provision to that effect in the contract of membership, but if not, the liability of all the members was limited. The directors were jointly and unlimitedly liable for the debts incurred during their management of the association.

The first step towards forming a *société en commendité* was the execution of a written contract of membership. The names of the members, the total amount of the capital,

the contribution of each member, etc., had then to be recorded with the Court. Only the directors had the right to call a general meeting of members. At a general meeting the consent of three-fourths of the members of the association was necessary before: (1) Any alteration could take place in the original contract of membership; (2) any decrease could take place in the capital; (3) any new member could be admitted; (4) any interest of the members with unlimited liability could be transferred; (5) any application of the member for retirement could be accepted; (6) any voluntary dissolution of the company could take place. Whenever three-fourths of the members passed a resolution touching any of the matters indicated, though the dissenting minority had no right to reject it, they had a right to retire on the ground that the original contract of membership had been altered.

The articles of association provided for the selection of directors, but anyone who by the articles assumed an unlimited liability, had a right to be a director, unless the articles expressly denied this right. A member of limited liability could only be appointed a director by a three-fourths majority of all the members. The directors prosecuted the business according to the original contract of membership. The members of unlimited liability could not transfer their interests in the company without the consent of three-fourths of all the members; but the interests of the members of limited liability could be transferred with the consent of the directors. With the consent of three-fourths of the association, members could voluntarily retire whether their liability was limited or unlimited. The involuntary retirement of a member could take place by expulsion, death, mental disability, and bankruptcy.

The causes of the dissolution of the association were substantially the same as in a *société en nom collectif*, except that the *société en commendité* might as stated be dissolved by a resolution adopted by three-fourths of the members at a general meeting, while a *société en nom collectif* could only be dissolved by the unanimous consent of all the members.

C. Société annonyme.

A *société annonyme* was an association in which the members were shareholders; that is, the capital of the association was divided into shares and any subscriber or transferee of the shares was only liable for the amount originally subscribed.

The preliminary steps in the organization of the *société annonyme* were the "Temporary articles of association and the affidavit. At least four persons, acting as promoters had to make the temporary articles and the affidavit. The purpose of the association, the number of shares and the amount of each share, had to be set forth in the affidavit. The temporary articles of association and the affidavit had to be sanctioned by the "authorities concerned." For instance, in case the business to be conducted was that of a bank, the temporary articles, would be sanctioned by the Financial Department, if a railway, by the Department of Communication. Before the articles had been sanctioned the public could not be asked to subscribe. After the total amount of the capital had been subscribed, a preliminary meeting of shareholders had to be called. The articles of association made by the promoters, the special interest or compensation they demanded, and the valuation of the property they subscribed, would be recognized, rejected or altered by this meeting. If the meeting had no objection to the articles of association prepared by the promoters they were affirmed.

On the conclusion of the preliminary meeting of shareholders, the promoters had to file the articles of association, the affidavit, the subscription books and the certificate of acknowledgement with the "authorities concerned." They then applied for a charter of incorporation. The *société* could not legally exist unless a charter was granted. The charter became invalid if the association was not recorded with the Court within one year after the grant. To register a charter at least one-fourth of the capital had to be paid. The effects of the registration were that: (1) The

formation of the association could be set out as a defence against third parties; that is those who claimed that a *société annonyme* did not exist, and that as a consequence all the members were jointly and severally liable; (2) the corporation could begin to prosecute its business; (3) the promoters, directors and shareholders could not be held jointly and unlimitedly liable for the debts; (4) the corporation could issue certificates of shares, and the shareholders could transfer shares to third parties. The corporation had to begin to presecute its business within six months after the registration.

From the point of view of its organization a *Société annonyme* consisted of three parts: the general meeting of shareholders, the board of directors, and the auditor or auditors. Both directors and auditors were appointed by the majority of the general meeting of shareholders. The corporate business was managed by the directors. The auditor was the overseer of the board of directors. He could inspect the corporate business and assets whenever he thought fit and report to the general meeting of shareholders.

The corporation was dissolved: (1) When the number of shareholders became less than seven; (2) on the happening of any event which had been designated in the article of association as causing a dissolution; (3) by a resolution of the general meeting of shareholders; (4) on the bankruptcy of the corporation; (5) when the capital had been decreased to such an extent that if all the debts were paid up, the amount of the remaining capital would be less than one-fourth of the amount of the original capital; (6) by an order of the Court.

4. THE PERIOD SINCE 1898 AND 1899.

In order to understand the present status of the Japanese law of association, it is necessary, as in continental Europe to understand the distinction between the Civil and Commercial law. The Civil Law is the general law; the Commercial Law embodied in the Commercial Code, is a

collection of exceptional principles which are designed to apply not to all commercial transactions, as most English and Americans would understand that term, but only to those within the scope of the code. While as stated a Commercial Code was adopted in 1893, the Civil Law was not embodied in a code until 1898.

The Civil Code of Japan consists of five books: 1. The Civil Law in General, such as the law of persons, things, the Statute of Limitations, etc. 2. The Law of Property. 3. The Law of Creditors and Debtors. 4. The Domestic Law. 5. The Law of Inheritance. The law of contract is a part of the law of creditors and debtors. The New Commercial Code of Japan consists of five books: 1. The Commercial Law in general, that is, the law concerning merchants, accounts, etc. 2. The Law of Association. 3. The Law of Commercial Transaction; that is the law which provides what are commercial transactions and to what extent the general rules of the Civil Code are not applicable to them. 4. The Law of Negotiable Instruments. 5. The Law of Shipping. The general law of association is dealt with as a branch of the law of contract in the Civil Code. What we have called Japanese partnerships are regulated by this Code. The other associations are creatures of the Commercial Code and are regulated solely by that code.

A. Partnerships.

A partnership under the Civil Code is defined as a contract between two or more persons making a common contribution for the purpose of carrying on a common enterprise. Thus, two elements are necessary to the validity of a partnership—the common contribution and the carrying of a common enterprise. If a party has not made any contribution, he cannot be held as a partner, though he may participate in profits. A partnership is always a co-ownership, but a mere co-ownership is not necessarily a partnership, since the co-owners may not carry on a common enterprise. A partnership is an association which does not require the action of government for its complete formation

It cannot sue or be sued in a partnership name, but must be proceeded against in the names of the individual partners. Since it is not in any sense an artificial person, it has no residence. Again, a creditor's right against the partnership could be set off against a debt due its individual members, and *vice versa,* if it were not for a special provision prohibiting such a set off. The partnership creditors have no priority against the partnership assets, the individual creditors of the partners having a right to compete for partnership assets with the partnership creditors. In case of compulsory execution, the sheriff can attach the partnership property at the suit of an individual creditor of a partner. A partnership may be either commercial or non-commercial. For instance, two or more gentlemen joining themselves together as a club, would be sufficient to constitute a partnership, if they made common contributions for the purpose of carrying on the common enterprise. Thus in the eye of the Civil Law of Japan, a philosophical society, if not organized under provisions of the Civil Code which provide for the special organization of religious, educational and scientific associations, is just as much a partnership as any business association.

Partnerships under the Civil Code are of course subject to the Civil Law. The differences between the legal effect of acts subject to the principles of the Civil Law and those subject to the principles of the Commercial Law enunciated in the Commercial Code are often radical. For instance, under the Civil Law the act of an agent of an undisclosed principle is presumed to be the act of the agent himself, but in a transaction subject to the Commercial Law the act of the agent is always binding on the undisclosed principal. The creditor's claim in Civil Law is barred in ten years, but in Commercial Law it is barred in five years. In the Civil Law the legal rate of interest is five per cent. per annum, in the Commercial Law six per cent. In the Civil Law a group of debtors are proportionately liable for their common debt but in Commercial Law they are jointly and severally liable.

Partnerships being subject to the Civil, not to the Commercial Law, it results from the rule of proportional liability just stated, that unless a joint liability is created by a special contract, a mere contract of partnership does not make the partners jointly liable for partnership debts, though each of them is unlimitedly liable for his own share of the partnership debts. If a partnership creditor is notified of the proportional liability between the partners, he cannot hold one partner for more than his share, but if not notified of the exact share, he has a right to assume that the share of each partner in the partnership is equal, and therefore that the liability of each partner will be equal.

B. Associations recognized by the Commercial Code.

In 1899 the new Commercial Code was adopted. This code recognizes four kinds of associations. All the associations formed under it must be business associations; that is associations organized with a view to profit. All the associations require the action of government for their complete formation, and when formed are regarded as legal persons distinct from their members. The new Commercial Code is based primarily on the German Commercial Code.

(*a*) *Société en nom collectif.* The same kind of association as the old *société en nom collectif,* though the law has been slightly changed.

(*b*) *Société en commendite.* A different kind of association from the old *société en commendité,* though the name is not changed.

(*c*) *Société annonyme.* The same kind of association as the old *société annonyme,* though the law has been slightly changed.

(*d*) *Société en commendite par actions.* The only kind of association which was absolutely unknown to the first code.

(*a*) *Société en nom collectif.*

The following are the characteristics of the new *société en nom collectif,* by which it can be distinguished from the old *société en nom collectif:*

1. The société is expressly recognized as a distinct legal person, while under the first code there might in some cases have been a doubt as to whether all *sociétés en nom collectif,* no matter what provisions were inserted in their articles, would be so regarded.

2. The incoming members are liable for the debts incurred before they are admitted to the membership, and this liability cannot be released by a special contract between the incoming member and the company.

3. The amount contributed by each member must be recorded in the Court.

4. Good will is recognized as contribution; that is if one of the members has an established business, which is taken over by the association, the value of the business may be regarded as part of the capital of the *société.*

5. The *société* can consolidate with any other *société* or *sociétés.*

6. The assets cannot be distributed to the members, before the debts have been paid.

In all other respects the association is the same as that of the *société en nom collectif* of the first Code.

(*b*) *Société en commendite.*

This is an association part of whose members are jointly and unlimitedly liable for the debts of the association, but the other part are only liable for the amount contributed. The law applicable to a *société en nom collectif* is applicable to this kind of association in the absence of special provisions. The requirements as to making the articles of association, and in respect to recording the articles with the Court are the same as in case of the formation of a *société en nom collectif.* The members of unlimited liability enjoy and assume the same rights and duties as the members of a *société en nom collectif,* but the members of limited liability have neither the right nor duty to manage the business of the company. Their only right relating to the business is the right to inspect the

books and assets. They cannot as part of their contribution contribute service or good will.

The members of unlimited liability can transfer their interests in the company with the unanimous consent of the members. The interests of the members of limited liability may be disposed of with the permission of the members of unlimited liability. The death or permanent insanity of a member of limited liability does not operate as a retirement of his interest. The *société* is dissolved either by the retirement of all the members of unlimited liability or that of all the members of limited liability; when all the members of limited liability retire, the société can be changed into a *société en nom collectif*.

The old *société en commendite* was abolished by the Japanese legislators on two grounds: first, the danger to that part of the public which might deal with the *société*, arising from the fact that all its members might be only limitedly liable; secondly, the impropriety and inconvenience of the existence of an association called *société en commendite* which was substantially different from the *société en commendite* of foreign countries. As will be perceived the new *société en commendite* follows in practically every detail the association of the same name in the German Commercial Code.

(*c*) *Société annonyme.*

There are several characteristics which distinguish the new *société annonyme* from the *société annonyme* of the first Code. In the first place the association need not be chartered by the "authorities concerned." Only registration in the Court is essential to its formation, a charter is not necessary. Neither need the articles of association be acknowledged by the administrative officers. In short, the new code recognizes the *société annonyme* as a voluntary association which can be formed by any group of persons competent to form associations under the Commercial Law.

In the second place the promoters may subscribe for the total amount of the capital without calling for any

other subscriptions. Where the promoters subscribe for all the shares they must apply to the Court to appoint a visitor for the purpose of determining whether one-fourth of the capital has been paid up; whether it is fair that the promoters may receive the special interest demanded; whether the property contributed by the promoters is not overvalued; whether the compensation for any service of the promoters is reasonable and necessary.

In the third place the general meeting of shareholders has a right to appoint an inspector. The duties of the inspector are fixed by law. He must inspect the books and accounts of the company submitted by the directors, and also the reports of the auditor or auditors, and he must inspect the corporate business and assets. Finally, when a general meeting of the shareholders is called by the auditor or auditors, he must inspect the subscription and payment of shares and the value of the property subscribed when new shares are issued.

In the fourth place the provisions intended to safeguard the public who are asked to subscribe are more elaborate than under the first Code. Each subscriber must fill up two blank forms which are provided by the promoters for the purpose if receiving subscriptions. These forms must state the following facts:

(*a*) The date on which the articles of association are made.

(*b*) The purpose and name of the association.

(*c*) The total amount of the capital and the amount of each share.

(*d*) The number of shares which must be owned by a director.

(*e*) The location of the principal and branch offices.

(*f*) How public notice of the association is given.

(*g*) The names and addresses of the directors.

(*h*) The number of shares subscribed by the promoters. moters.

(*i*) The amount which should be paid in before the preliminary meeting of shareholders.

The names and addresses of the auditors must be registered in the Court. The issue of bonds must also be recorded. If shares of stock have been fully paid up, they can be changed into unsigned shares, unsigned shares being transferred like negotiable instruments. The association can consolidate with any other similar association. The assets cannot be distributed even in good faith, before the debts have been paid.

(*d*) *Société en commendité par actions.*

This société like the *societe en commendite* is an association consisting of members of limited and members of unlimited liability. The difference between the members of unlimited liability and those of limited liability is the same as in the case of a *société en commendite,* but the limitedly liable members of this association hold transferable shares like the shareholders of a *société annonyme.*

The advantages of this kind of an association are marked. The members of a *société en commendite,* even of limited liability, cannot freely transfer their shares, but the shareholders in the *société en commendite par actions* may dispose of their interests whenever they like. On the other hand, the directors of a *société annonyme* usually have a tendency to neglect the business at the expense of shareholders, but the members of unlimited liability in this association having by the fact of their liability a greater personal stake in the association, are more apt to manage its business with care.

The association is partly subject to the rules relating to *société en commendite* and partly to those relating to the *société annonyme,* but there are certain provisions applicable only to this kind of association. Thus, when the association is formed, all the members of unlimited liability should act as promoters, makng the articles of association and calling for subscribers. The promoters though they may subscribe for some of the shares, cannot subscribe for

all of the shares as the promoters of a *société annoyme.* Again, the shareholders at the preliminary meeting appoint the auditors, but not directors, because the members of unlimited liability have the right and duty to manage the business of the société. The directors may attend the general meeting of shareholders and express their opinions, but they have no right to vote. The auditor is the overseer of the shareholders as well as of the directors, though he must be chosen from the shareholders. It is the duty of the auditor to urge the directors to act according to the resolutions of the general meeting of shareholders, if the resolution has been recognized by the members of unlimited liability.

C. The Old Société Commendite.

The general rule for carrying out the law of association under the new Commercial Code is, that the commercial associations which were formed before the new Commercial Code came into operation, are subject to the new Commercial Code. But there are several exceptions to this rule the most important being that the *sociétés en commendite,* formed under the Code of 1893, where they continue to exist, are still subject to the provisions of the first Commercial Code.

The business associations known to the Japanese law are therefore six in number. The partnership of the Civil Law, the four associations recognized by the Commercial Code, and the *Société en Commendite* organized under the first Commercial Code. Indeed, this *société en commendite* under the Code of 1893, is still the most popular form of business organization though, of course, no new organization of this kind can now be formed.

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(To be continued.)