NISHIMURA
& ASAHI

The Corporate Counselor

- Insights into Japanese Corporate Law -

April 2015/No.19

STOMPING OUT SEXUAL HARASSMENT AND DIRECTOR RESIDENCY REQUIREMENTS IN JAPAN: *OLYMPIC CHANGES*

This edition of the *Corporate Counselor* provides important updates on topics covered in two of our most popular newsletters: (i) legal issues associated with challenging sexual harassment in Japan, and (ii) matters to consider when establishing a company in Japan. While these topics are vastly different, the updates share a common theme – international norms appear to be influencing the enforcement and enactment of Japanese laws and regulations.

Many developed countries have comprehensive schemes to combat sexual harassment, and the corporate laws of few industrialized countries have director residency requirements. Japan is gradually progressing from being a back-marker in this regard to running with the pack.

Update on Putting an End to Sexual Harassment in Japan

On February 26, 2015, Japan's Supreme Court upheld the decision by the operator of Osaka Aquarium Kaiyukan (the "Company") to take stringent disciplinary action against two male managers for repeatedly engaging in sexually harassing conduct towards two female co-workers over a period of approximately one year. The landmark decision by Japan's Supreme Court should provide aggrieved employees with a meaningful avenue to redress sexual harassment claims in light of impediments in the Japanese legal system (as more fully explained in our 2013 overview of sexual harassment claims in Japan, which is available by clicking here).

According to the Supreme Court's holding, from November 2010 to December 2011, a male manager made various lewd comments to a female subordinate when alone with her in the workplace, including providing unsolicited detailed descriptions about (i) his extramarital affairs with women around the same age as the subordinate, (ii) the dimensions of his reproductive organ, (iii) his increasing sexual appetite, and (iv) the type of women he found attractive. Over the same time period, another male manager continuously berated two female subordinates, one of whom was the same person as the above subordinate, that they should get married soon as they risked becoming old mistresses and repeatedly suggested that they take up night-time employment to earn extra money (presumably made with nefarious overtones).

In December 2011 one of the female co-workers lodged a sexual harassment complaint with the Company about the managers. After holding an internal investigation, the Company decided to suspend one manager for 30 days, transfer him to another department, and demote him by one rank (allegedly causing him an aggregate loss in salary, bonus and benefits of approximately JPY25 million, assuming he remained with the Company until his retirement), and the Company decided to suspend the other manager for 10 days, transfer him to another department, and demote him by one rank (allegedly causing him an aggregate loss in salary, bonus and benefits of approximately JPY20 million, assuming he remained with the Company until his retirement). The managers complained that the Company's disciplinary action was unduly harsh because the female co-workers did not indicate that they found the conduct offensive, the managers were unaware of the Company's policies against sexual harassment, and the managers were not otherwise given advance notice that their respective conduct was sexual harassment and contrary to Company policies. The Company was not swayed by such arguments, and the managers took the Company to court.

The Osaka District Court ruled that the disciplinary actions imposed by the Company were appropriate because the managers' comments were obscene and malicious and the female co-workers were particularly vulnerable because they were employed on short-term fixed contracts. The managers appealed the Osaka District Court's decision, and the Osaka High Court ruled in their favor by holding that the punishment was overly harsh in light of the circumstances. The Company appealed the Osaka High Court's decision to the Supreme Court of Japan.

The Supreme Court of Japan reversed with prejudice the decision of the Osaka High Court and held that the punishment imposed on the managers was reasonable and not an abuse of the Company's disciplinary authority. The Supreme Court noted that the statements made by the managers were extremely inappropriate and caused the female employees to experience a sense of disgust and humiliation. The managers should have naturally known, in light of their managerial responsibilities, that their conduct was offensive without needing any advance warning from the women or the Company. Furthermore, the Supreme Court held that the managers' claims of not knowing the Company's policies against sexual harassment were spurious and not mitigating factors. The Supreme Court reasoned that the Company clearly treated the prevention of sexual harassment at the workplace as an important issue by obligating all of its employees to participate in periodic sexual harassment training sessions, and by distributing to all of its employees pamphlets denouncing sexual harassment.

The Supreme Court's holding in the *Kaiyukan* case is noteworthy because it suggests that judicial review is inappropriate over an employer's disciplinary action decisions made under the cover of Japan's Equal Employment Opportunity Law, so long as reasonable internal due process procedures have been followed. As more fully explained in our 2013 overview of sexual harassment claims in Japan,

Stephen D. Bohrer

Foreign Law Partner
03-5562-8648
s_bohrer@jurists.co.jp

Miki Fujita

Partner
03-5562-8388
m_fujita@jurists.co.jp

Article 11 of Japan's Equal Employment Opportunity Law imposes an affirmative obligation on an employer in Japan to prevent sexual harassment from occurring in the workplace. The Company took seriously its obligation to prevent sexual harassment in the workplace by distributing to all of its employees documentation explicitly stating that sexual harassment would not be tolerated and by obligating all of its employees to participate in annual sexual harassment sensitivity training sessions. When the managers at issue failed to adhere to the Company's warnings, the Supreme Court permitted the Company to impose upon these managers the second harshest disciplinary punishment available under the Company's work rules (the first being employment termination) after an internal investigation of the alleged misconduct was completed. Had the Company not adequately investigated the veracity of the claims, perhaps the judicial outcome would have been different.

With the current lack of judicial precedents in Japan where an individual has directly pursued a sexual harassment claim, combined with the modest monetary damages that have been awarded in the few court precedents (which most likely could not have even covered the aggrieved employee's litigation costs), providing an employer with a roadmap to eradicate sexual harassment is an important step towards eliminating such conduct in the Japanese workplace and may have the bonus effect of providing aggrieved employees with a potential avenue to redress sexual harassment claims in a cost-effective manner. After all, the employer incurs the time and expense to assess its desired disciplinary action and to defend any challenges to its decision (which hopefully it will vigorously pursue). Aggrieved employees also may eventually directly benefit if employer-sanctioned disciplinary action is aggressively pursued and not routinely overturned. Specifically, deference to an employer's disciplinary action decision implemented after the completion of reasonable internal due process procedures could serve as *prima facie* proof that sexual harassment did occur, thereby providing an aggrieved employee with a stronger case should a civil suit be initiated.

Update on Eliminating Residency Requirements

Foreign direct investment into Japan recently became easier to complete. On March 16, 2015, Japan's Ministry of Justice announced that it was repealing its long-standing local residency requirement, which often complicated the corporate formation process for overseas entrants into Japan. The change became effective immediately.

Historically, a Japanese company formed as a *kabushiki kaisha* (the equivalent of an ordinary corporation or "c-corporation" in the United States and currently the most common corporate form in Japan) was required under Japanese law to appoint from among its directors at least one individual who was a resident of Japan to serve as the company's (i) Representative Director (for a *kabushiki kaisha* having a board of directors corporate governance scheme) or (ii) local representative (for a *kabushiki kaisha* having a director without a board of directors corporate governance scheme). Similarly, a *godo kaisha* (the equivalent of a limited liability company/LLC in the United States) that has an entity serving as its sole managing member was required to select at least one individual who was a resident of Japan to serve as an executive officer to perform the duties of the managing member. While the foregoing residency requirements may appear innocuous on their face, in practice they often caused headaches for overseas entrants to Japan because such companies frequently could not attract the requisite personnel until its corporate infrastructure was established (thereby creating a painstaking conundrum because corporate formation formalities required the retention of a Japanese resident, but an overseas company often could not attract such qualified Japanese residents until the company was established). To overcome this dilemma, new entrants to Japan often paid large fees to local service providers in order to supply Japanese residents on an interim basis to satisfy corporate formation formalities. This will no longer be required.

Effective immediately, a company can be organized under Japanese law without the need to satisfy any Japanese corporate law local residency requirements.

Although it could be difficult to operate a business in Japan without a local leadership team, the elimination of local residency requirements should be cheered by overseas companies that desire:

- to initially utilize home office personnel to serve as leaders of its Japan subsidiary until a local talent search can be completed and the Japan business model can support the hiring of local personnel; and

- not to heed local residency requirements when filling vacancies or implementing business plans to provide direct overseas oversight.

The elimination of local residency requirements for directors (in relation to a *kabushiki kaisha*) and executive officers (in relation to a *godo kaisha*) applies only with respect to Japanese corporate law formalities. The elimination is not a blanket waiver under all Japanese laws. Therefore, companies operating in certain regulated industries in Japan may still need to comply with local residency requirements due to industry regulations and licensing requirements.

The July 2012 edition of the *Corporate Counselor* highlighted the principal differences between a *kabushiki kaisha* and a *godo kaisha*, and suggested factors to consider when selecting a corporate form for a subsidiary in Japan. We have updated our prior newsletter to take into account the recent elimination of local residency requirements under Japanese corporate law. The updated newsletter is available by clicking here.

* * * *

Why is the Japanese judiciary suddenly adopting a more stringent view against sexual harassment and a Japanese ministry removing restrictions to facilitate subsidiary formation in Japan by overseas companies? No one can say for sure, and we would like to add another theory to the mix.

As we draw closer to the 2020 Tokyo Olympic Games, the

world's spotlight will be on Japan and many aspects of Japanese society will be viewed under a microscope. Antiquated views could be subject to ridicule and historical practices that have uneven consequences could be taken as discrimination. Clearly, not the image Japanese leaders want portrayed to the world.

Eliminating sexual harassment and regulatory red-tape is a multi-year project, so it is not surprising that these important areas have received remedial action at this early stage. If the *Olympic Change* theory is correct, then we will see many more transformative changes to Japanese laws and regulations over the next five years. Conducting business in Japan may never be more dynamic and attractive!

Nishimura & Asahi
Ark Mori Building, 1-12-32 Akasaka, Minato-ku, Tokyo 107-6029, JAPAN
Phone：81-3-5562-8500 Fax：81-3-5561-9711 URL：http://www.jurists.co.jp/en/