Baker McKenzie.

Dispute Resolution
Tokyo

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Force majeure under Japanese law

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1. Introduction

In light of recent global events, parties' ability to perform obligations under commercial contracts is being stretched or, in certain cases, made not only commercially impractical but also objectively impossible. This will likely increasingly be the case given the as-yet-unknown end point and future extent of the coronavirus, including from the standpoint of geographical reach.

When faced with such circumstances, parties in cross border commercial relationships often seek to rely on remedies available for so-called force majeure events, either set out in contracts or stipulated in the laws of relevant jurisdictions, or both. The function of these remedies is to provide parties with relief when certain events occur which are outside of a party's control that render contractual performance impossible, difficult or onerous. Should such clauses exist in a contract or should such remedies be offered as a matter of law, a party may be excused from, allowed to suspend, or permitted to modify all or part of its contractual duties and may be released from liabilities due to breach, default or delay.

In this client note, we explore the concept of force majeure and similar doctrines under Japanese law and whether force majeure clauses in commercial contracts are enforceable in Japan. Further, we address certain practical considerations for those seeking to ascertain how the force majeure remedies may apply to their own circumstances.

2. Are force majeure clauses enforceable under Japanese law?

Under Japanese law, the principle of freedom of contract between parties, by which they may agree to contractual terms with little or no statutory control or interference from the courts, is generally upheld. As such, while Japanese law does not provide expressly for a rule of force majeure in the Civil Code of Japan or elsewhere,[1] it does not prevent parties from agreeing to include such clauses and remedies in their contracts.[2] Accordingly, force majeure clauses in commercial contracts are ordinarily held as enforceable agreed terms by the Japanese courts.

Force majeure clauses typically recognized and deemed enforceable in Japan entitle a contract party to certain special remedies if and when an unexpected

[1] The Civil Code of Japan makes reference to force majeure in Clause 3 of Article 419, which provides a non-mandatory rule that monetary obligations, including damages for breach of contract, may not be excused on grounds of force majeure. This is an exception to the general rule under Clause 1 of Article 415, which denies liability for damages due to failure to perform a contractual obligation if the failure is caused by a reason not attributable to the obligor. Practically speaking, however, these are voluntary rules and apply only if the point of issue has not been otherwise addressed in the contract between the parties.

[2] There are a very limited number of court cases in which obligations, not including those related to payment, have been waived or modified due to certain limited types of force majeure events (such as large earthquakes and extreme storms) despite the related contracts not containing force majeure clauses. These cases are, however, extremely rare.

and uncontrollable event occurs, to the extent that such event makes performance of that party's contractual obligations impossible or almost entirely impractical. These remedies include:

- rescission of an order or voiding a contract;
- adjusting the scope or steps for performance, such as timing and method of delivery;
- forfeiture of paid-in-advance costs, fees or price (release from refund obligation); and
- excusing a breach of contract, waiving an obligation or otherwise releasing a party from liability.

While no published case exists in which a force majeure clause was in dispute and presented to a court for its decision, it is foreseeable that a Japanese court, when interpreting a force majeure clause, would generally determine the remedies and scope of the clause with reference to the specific contents therein. Japanese courts' interpretations of contract clauses are often fairly strict and will focus primarily on the explicit wording of the contract, although judges may also take into account various factors outside a written agreement. These factors include the contents of correspondence and communications between the parties, which a judge may consider to ensure reasonable interpretation of a clause if a strict reading of it does not make logical sense in light of the entirety of the contract and the objectives of the parties.

Whilst force majeure clauses in commercial contracts are understood to be generally enforceable in Japan as set out above, there are certain restrictions imposed under mandatory rules of Japanese law. Rules that may have an impact on the extent of the enforceability of force majeure clauses include:

- the duty of good faith and anti-abuse of rights rules, which will require a party claiming force majeure to (i) be fair and reasonable in seeking remedies; (ii) limit its remedies to the minimum necessary to save significant and unexpected detriment; and (iii) not take advantage of a situation by claiming excessive remedies[3];
- public order rules, which may deny or limit enforceability of specific force majeure clauses to the extent necessary to protect the public order of Japan[4]; and
- consumer protection laws applicable to business-to-consumer (B2C) transactions and fair competition law intended to protect small suppliers and vendors from unfair business practices, which may deny or limit the effect of certain force majeure clauses.

Separately, force majeure clauses in contracts governed by Japanese law may be affected by certain voluntary rules under Japanese contract law if a given contract does not expressly or impliedly exclude statutory remedies.[5]

3. Remedies where a contract does not contain a force majeure clause

Even where a contract does not contain a force majeure clause, or where a clause exists but does not provide for the type of remedy needed by a party,

[3] Article 1 of the Civil Code of Japan.
[4] Article 90 of the Civil Code of Japan.
[5] For example, Article 419, Clause 3 of the Civil Code of Japan.

there are a small number of doctrines under Japanese statutory and case law offering similar remedies in limited circumstances.

Examples of these doctrines include the rule of impossibility (*rikou hunou*), the rule of exemption from breach of contract liability due to a reason not attributable to the breaching party (*saimusha no seme ni kisubeki jiyuu ni yoranai saimu furikou*) and the doctrine of significant circumstantial change (*jijou hennkou no housoku*).

Under Japan's Civil Code, the rule of impossibility allows a party to a contract to be released from an obligation to perform where that performance is "impossible" in light of social common sense.[6] Proving impossibility under this rule, however, is difficult given that the obligor must show that performance is impossible objectively and permanently.

A party defaulting on its contractual obligations will be liable for damages caused by its non-performance regardless of whether the performance is possible or impossible, but such liability will be waived if and to the extent that the non-performance was caused by a reason neither foreseeable or attributable to the party.[7]

An exception to these rules is the obligation to pay money and liability for breach of money-payment obligations. This obligation and liability will not be released or waived even if there is an event of force majeure.[8] In other words, the money payment obligation and liability for default on said obligation will be released only if the obligation is not performable due to a reason attributable to the other party (e.g., refusal to accept or impossibility of receiving the payment).

The Japanese courts have also established the doctrine of significant circumstantial change, which permits a contract party to unilaterally amend or rescind a contract if there is a significant unexpected change in social circumstances, such as nationwide hyperinflation.[9] These remedies would only be allowed insofar as the change alters the essential assumptions and fundamental underlying facts of the contract, such that performance may be possible but would be extremely unjust as a matter of fairness between the parties. Again, there are a very limited number of court decisions pertaining to this doctrine.

4. Practical considerations

Any party that has entered into a commercial contract that has been, or may be, affected by an event of force majeure such as the coronavirus should:

- review the relevant contract carefully, particularly with regard to the governing law and force majeure provision, together with any procedural requirements or time restrictions;
- consider whether the force majeure clause contains an exhaustive list of force majeure events (e.g., specific events such as epidemics and/or pandemics as qualifying events of force majeure) or is more "open."

[6] Article 412-2 of the Civil Code of Japan.
[7] Article 415, Clause 1 of the Civil Code of Japan.
[8] Article 419, Clause 3 of the Civil Code of Japan.
[9] The first ruling related to this doctrine was in a 1944 Imperial Supreme Court judgment.

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- analyze possible remedies under Japanese law and assess the interaction between the contract and the statutory remedies in order to identify the applicable force majeure remedy;
- review the factual background and details of the specific issues to see if the identified remedies are triggered in a particular case and, if so, what steps must be taken or pre-conditions satisfied to invoke the remedies;
- should you wish to utilize a force majeure clause, consider whether you are obliged to mitigate the effect of non-performance and what steps you may be able to take to do so; and
- consider the future consequences of invoking a claim for force majeure, such as whether this may lead to termination of the contract.

Aside from the position under the contract, there will likely be several other salient matters to consider, including the following.

- Overall, consider business solutions and commercial approach leveraging with regard to your legal position.
- Where a party receives a claim for force majeure but considers it invalid, the issue of enforcement of the contract may arise. This consideration may be particularly acute where international arbitration is not provided for in the contract.
- The reputational risks and potential damage to long-term supply relationships that may be caused should be considered. Here, even where a party considers a force majeure claim to be without basis, it may be advisable to remain flexible with regard to amending or restructuring the contract.
- The impact a claim for force majeure may have on the parties' insurance arrangements should be considered.
- Where a claim for force majeure is made by a party as part of a chain of supply contracts, there may be knock-on effects on other obligations in the chain. As such, a buyer in a chain may need to declare force majeure in response to its supplier doing so.

5. Conclusion

During the coming months and perhaps beyond, parties are likely to find themselves exposed in some capacity to difficulties in the performance of obligations within their commercial relationships, whether that be their own performance or that of others in their supply chains. Where this occurs, parties should consider the extent to which they, or their counterparties, may be able to rely on remedies under force majeure clauses contained in contracts or similar doctrines and rules under Japanese law.

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If you would like to discuss any of the issues raised in this alert, please contact us.