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ARTICLE

The Law and Reality of Custom in a Civil Law Country: Experiences of Japan

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1. Introduction

Custom and usage are norms generated from non-state sources. While their usefulness in filling the gaps in the national legal system and interpreting contracts are widely recognised, their existence is the exception to the general assumption of the modern legal system that the state monopolises the power to make laws. The custom and usage as non-state norms may not always be consistent with the policies and goals that the state as the legislator pursues. On the other hand, one of the basic principles of modern commercial law is private autonomy. From this perspective, admitting and enforcing the rules that the private community develops is even the requirement under the basic principle of the modern commercial law. Thus, one must examine how the courts handle the custom and usage in actual cases in their efforts to smooth out the uneasy coexistence of custom and usage and the national Codes and statutes.

Theoretically, there can be two approaches to addressing the issue of custom and usage versus state law. One possible approach is that state law accepts custom and usage as an alien element to a certain extent. The other approach is to affirm the relevance of custom and usage subject to some level of judicial control. Both approaches may, in practice, be varied depending on the extent to which state law accepts the alien norm or the extent of judicial control. Furthermore, the two approaches could be combined and employed simultaneously. It is anticipated that the choice of approach reflects the role of state law in society, which differs across jurisdictions.

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This article considers the above issue with a specific focus on Japan. More precisely, it examines how Japanese courts have struggled to find the right place for custom and usage in Japanese law. It is not intended to assert that there is a clear-cut Japanese approach as distinguished from other approaches in other jurisdictions. Rather, the Japanese Civil Code is a product of legal transplant in the late nineteenth century and has since then developed due to the localisation efforts of academic doctrine and court practices. Such doctrine and practices have, on their side, been subject to foreign influence, as the 'reception' of foreign doctrine and case law.[1] Against these backgrounds, local custom and usage could have different roles in Japan from those they have in Europe. For example, they could ensure that the transplanted Code is smoothly accepted by, and applicable to, *Japanese* society.

The remaining part of this article is structured as follows. After describing the apparent complications in the rules on custom under Japanese law, the relevant rules and their historical origins are explained ('Section 2'). Then, several cases in which the court discussed customary law and usage are reviewed to examine the function of custom and usage in practice ('Section 3'). This review is followed by an analysis of the court's approach towards customary law and usage ('Section 4'). The concluding part ('Section 5') sums up Japan's experience with custom and usage, and briefly discusses a few remaining issues. The scope of this article is limited to commercial transactions; customs concerning the traditional use of land, water or fishery resources are not considered.

2. Custom and usage under Japanese law

2.1 Legal framework and terminology

The legal framework in Japan to address the status of custom and usage is seemingly inconsistent. On the one hand, the Act on Rules for the General Application of

[1] On the transplant of black-letter law provisions and the reception of academic theories that followed in Japan, see Luke Nottage, 'Development of Comparative Law in Japan', in Mathias Reimann and Reinhard Zimmermann (eds), *The Oxford Handbook of Comparative Law* (2nd edn, OUP 2019) 201.

the Laws (ARGAL), which is the basic statute dealing with choice of law rules, provides that the '[c]ustoms which are not against public policy shall have the same effect as laws, to the extent that they are authorised by the provisions of laws and regulations, or they relate to matters not provided for in laws and regulations'.[2] Thus, the ARGAL limits the applicability of customs in two respects. The custom must not be contrary to public policy, and its subject matter must fall under the lacunae of the laws and regulations, unless they otherwise authorise the custom to apply. In other words, statutory rules ('laws and regulations') override customs.

On the other hand, the Civil Code appears to admit the applicability of custom more generously. It provides that the 'custom which is inconsistent with a provision in any law or regulation not related to public policy' shall prevail 'if it is found that any party to a juristic act (*hôritsu kôi*) has the intention to abide by such custom'.[3] Here, as far as the juristic act (contract) is concerned, the custom prevails over non-mandatory rules of the Code or statute ('law or regulation not related to public policy'). The only conditions are the parties' will (intention) to abide by the custom and the custom's compatibility with the mandatory law.

The third rule on customs is included in the Commercial Code. That Code applies to 'commercial matters.' It provides that a commercial matter-relevant subject that is not addressed by the Commercial Code is to be 'governed by the commercial custom', and that if there is no commercial custom, the subject is governed by the Civil Code.[4] Here, commercial custom prevails over the Civil Code as far as commercial matters are concerned.

The above seemingly inconsistent legal framework has become even more difficult to understand because of complications in terminology that academics introduced after codification. The Codes in Japan only mention 'custom' (*kanshû*). However, commentators

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[2] Art.3, Act on Rules for the General Application of the Laws (ARGAL).
[3] Article 92 of the Civil Code. 'Juristic act' is the translation of *Rechtsgeschäft* in the German Civil Code and is in most cases equivalent to a contract.
[4] Art. 1(2), Commercial Code. There used to exist further complications, because, until 2005, the Commercial Code mentioned 'commercial customary law' (*shô kanshû hô*). Given that this term has now been replaced by the phrase 'commercial custom' (*shô kanshû*), one may ignore the addition of the word 'law' in the previous text of the Commercial Code and understand 'commercial customary law as the equivalent of 'custom' (in the sense of legal obligations) concerning commercial law subjects.

distinguish between 'customary law' and 'custom as a fact'. On the prevailing view, customary law requires a sense of legal obligation (*opinio juris*), and practice without such a sense remains custom as a fact.[5] Thus, 'custom as a fact' is equivalent to what is known as 'usage' in other jurisdictions.

Though not found in the Codes and statutes, courts and commentators sometimes use the term 'practice' (*kankô*). It is against this background that, when Japan became a party to the United Nations Convention on Contracts for the International Sale of Goods (CISG), 'usage' and 'practice' in Article 9 (1) were translated as '*kanshû*' and '*kankô*' respectively.

2.2 The origins of the complications and inconsistencies

The seemingly inconsistent rules are the product of compromise in the process of drafting the Codes.[6] When Japan's Civil Code was drafted, as part of an effort to modernise the Japanese legal system, there were three leading drafters: Nobushige Hozumi, Kenjiro Ume and Masaakira Tomii. The three also drafted the Law on the Application of Laws (known by its Japanese name, '*Hôrei*'), the predecessor to the current ARGAL. The records show that Ume and Tomii held opposing views on custom. Both had studied at the University of Lyon before being engaged to draft *Hôrei* and the Civil Code, so both were familiar with modern codification in European countries, especially France.[7] Tomii argued that the Civil Code should replace the ambiguous customary rules with clearly drafted rules in order to establish people's rights. Against his argument, Ume advocated broader application of custom, pointing to the difference in the backgrounds of codification in

[5] Sakae Wagatsuma, *Shintei Minpô Sousoku* (The General Rules of the Civil Code, revised) (Iwanami Shoten 1965) 17, 252 (in Japanese); Yoshiyuki Noda, *Introduction to Japanese Law* (Anthony H Angelo tr, University of Tokyo Press 1976) 219.
[6] The following description is based on Eiichi Hoshino, 'Hensan Katei kara Mita Minpô Shûi' ('A few issues on the Civil Code observed from the drafting process'), in *Minpô Ronshû* ('Essays on the Civil Code') vol 1 (Yuhikaku 1970) 151 (in Japanese).
[7] Béatrice Jaluzot, 'Tomii et Ume, quand la faculté de droit de Lyon forme les rédacteurs du Code civil japonais', in Béatrice Jaluzot (éd), *Droit japonais, droit français: Quel dialogue?* (Schulthess 2014) 5.

France and Japan. While in France the Civil Code was codified on the basis of existing local customs, the drafters of the Japanese Civil Code had not taken the same approach. Though a limited attempt was made at such an approach, it was not easy to identify Japanese local customs in a short period of time. As a result, codification in Japan was based on the Western model.

In fact, the Ministry of Justice had published the Collection of Civil Customs (*Minji kanrei ruishû*) the year before, followed by the National Collection of Civil Customs (*Zenkoku minji kanrei ruishû*) in 1880. They were based on research conducted in 1876. However, lawyers and judges tended to consider the customs collected therein irrelevant to legal decisions and did not pay much attention to them.[8] This perhaps explains why, as Ume remarked, it was difficult to identify legally meaningful customs.

In the end, the drafters reached a compromise. The additional requirement of the parties' will to abide by custom has been inserted into the Civil Code to narrow the applicability of custom, reflecting Tomii's argument. *Hôrei*, whose rule on custom and statutes was exactly the same as the current ARGAL's, left it unclear whether custom is subject to any statutory rules, including non-mandatory rules, or only to mandatory rules.

The two opposing views must be understood in their context. In 1890s Japan, at that time, codification meant legal transplant. Tomii tried to perfectly transpose the purpose that the original codification had in the European context: namely, nation building.[9] In Europe, the Civil Code replaced local customs, as national power integrated the local powers into a modern nation state. If one assumed that the purpose of codification in Japan was the same as that in France or Germany, Tomii's argument could be convincing. However, Ume noticed the differences in context. In Japan, codification was motivated by the desire to equip a state newly opened to the global market with a modernised legal system and thereby impress the West, showing it that Japan was more than an equal

[8] Kazuhiro Murakami, 'Saiban Kijun toshiteno "Shûkan" to Minji kanrei ruishû' ('The "custom" as criteria for judicial decisions and the Collection of Civil Customs'), (1998) 49 (5) Dôshisha Hougaku 290 (in Japanese).
[9] Mathias Siems, *Comparative Law* (2nd edn, CUP 2018) 51.

counterpart.[10] However, the idea of a civil code was foreign to a society that had started Westernisation in 1869. In Ume's eyes, local custom was needed to bridge the gap between the Code and society and ensure that transplanted law was adequate and appropriate to a uniquely Japanese context. Thus, the opposing approaches to custom reflected the divergent views about the purpose of codification.

There was also the global context. The Japanese Civil Code was approved by Parliament in 1898. After the turn of the century, the Civil Code of Switzerland provided in its Article 1 '[i]n the absence of a provision [in the Code], the court shall decide in accordance with customary law and, in the absence of customary law, in accordance with the rule that it would make as legislator.' In contrast to the idea that prevailed in the eighteenth and nineteenth centuries, the more liberal approach to customary law was emerging. The Japanese Civil Code was not alone in this respect.

2.3 Custom before codification

In fact, reference to custom as a legal source had been allowed under the law even before the drafting of the Civil Code commenced. In 1875, eight years after the Meiji Restoration, the *Dajokan* (Great Council of the State) published Proclamation No.103 of 1875.[11] In this notice, the *Dajokan* pronounced that judges were to decide cases pursuant to statutes, which were being enacted in a fragmentary manner, and to refer to custom and reason when no relevant statute existed. Several cases that applied custom and usage are reported before the codification of the Civil Code.[12] As observed by Ume, custom, like equity in common law legal systems, already played the important role of filling the gaps between the statutes copied from Western laws and life in Japanese society.

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[10] On the history of early law making in Japan, see Kenzo Takayanagi, 'A century of innovation: the development of Japanese law, 1868-1961', in Arthur Taylor von Mehren (ed), *Law in Japan* (Harvard UP 1963) 5; Hiroshi Oda, *Japanese Law* (3rd edn, OUP 2009) 13.
[11] On this Proclamation, see Noda (n 5) 187.
[12] Murakami (n 8) 295.

2.4 The approach to custom after codification

Slight complications were added afterwards by the doctrinal transplant. In 1915, Terumichi wrote an article and pointed out that the Japanese Civil Code lacked an express provision on the interpretation of a contract (to be more precise, juristic act). He then argued that Article 92 of the Civil Code impliedly dealt with contractual interpretation. According to Terumichi, Article 92 of the Civil Code, though it only addresses the meaning of custom on its face, should be understood as equivalent to Articles 133 and 157 of the German Civil Code, in that it excludes the literal interpretation of a contract. If such an argument is to be accepted, 'custom' in Article 92 of the Civil Code should be 'custom as a fact' (usage), as distinguished from customary law as the source of law.[13] This argument has become popular and developed into the prevailing view mentioned above.

Indeed, the approach that the judge should give effect to the true intention of the parties over the letter of the contract has become popular in Europe. Usage is usually named as one of the factors that the judge should consider in interpreting a contract, as in the European Principle of Contract Law ("PECL"), Articles 5:101 and 5:102, and the Draft Common Frame of Reference ("DCFR"), Articles II.-8:101 and II.-8:102.[14] With the knowledge of such developments a century later, one may say that regarding a Code's provision on the effect of custom as implying a general principle of liberal interpretation of a contract makes sense. However, it should be noted that the text of Article 92 of the Japanese Civil Code is ambiguous in its nature, as opposed to the two provisions in the German Civil Code that Terumichi mentioned. The ambiguity of the Japanese Civil Code derived from the different context in Japan, as discussed above. In other words, Terumichi transplanted the German legal doctrine to Japan, despite the divergence in the texts and despite the differences in context.

[13] Bungei Terumichi, 'Hôritsu Kôi no Kaishaku (Minpô 92-jo)' ('The interpretation of a juristic act: article 92 of the Civil Code'), (1915) 10 Kyoto Hôgakukai Zasshi 293, 316-317.
[14] See also Unidroit Principles of International Commercial Contracts ("UPICC"), Article 4.3, which includes usage in the circumstances relevant to the interpretation of a contract, though the UPICC does not endorse the pursuit of parties' true intention over the letter of a contract.

3. The court's approach towards custom and usage

3.1 Customary law and usage under case law

In order to see how usage works in practice, one must examine actual court decisions. On a theoretical level, the Great Court of Judicature (the predecessor to the Supreme Court before the Second World War) accepted the distinction between customary law (supported by the *opinio juris*) and custom as a fact (usage). It established that Article 92 of the Civil Code addresses custom as a fact, while Article 2 of *Hôrei* provides for the applicability of customary law.[15] In fact, however, the courts have been restrictive in affirming the existence of customary law (to be applicable pursuant to *Hôrei*). There are not many cases that used custom as a source of law to fill the gap between the text of the Civil Code or Commercial Code and life in Japanese society, as was envisaged by the drafters. This may not be surprising. As Japanese society changed, the gap, assuming it ever existed, between the Code's text and life in that society, may have quickly disappeared.

On the other hand, the courts were more open to finding custom as a fact (usage). According to Article 92 of the Civil Code, custom (which is understood as custom as a fact) is relevant only when the parties have the will to abide by it (see 'Section 2.1' above). Then the question is how the court identifies the parties' will in an individual case. The Great Court of Judicature held that parties are presumed to have the intention to abide by the usage when the usage exists and the parties are aware of it.[16] As a result, the requirement under the Civil Code does not pose an impediment for the courts to find custom as a fact (usage) relevant. While leaving the room for parties to explicitly exclude the application of usage or to rebut the presumption of having the intention to abide by the usage, thus respecting the party autonomy, Japanese courts treat the party's silence as the presumed consent to be bound by it. This approach has enabled the courts to not exclusively focus on the parties' contract but to consider all the circumstances of the case, including

[15] Great Court of Judicature, 21 January 1916, *Minroku* vol 22, 25.
[16] Great Court of Judicature, 2 June 1921, *Minroku* vol 27, 1038.

those evidenced by the expert witness, in identifying the existence of usage in many cases (as in cases elaborated in 'Section 3.3' and 'Section 4.2' below).

3.2 Cases determining commercial customary law

Some of the cases that determined commercial customary law related to negotiable instruments. In a few cases, the measure to transfer the named certificate of shares of a joint stock company was the issue. The corporate law before 1938 (as codified then in the Commercial Code) provided that the transfer of a named share certificate was valid against the issuing company and other third parties only after the name and address of the acquirer were registered in the registry of shareholders.[17] However, in practice investors ignored this process and simply handed the certificate to the assignee with the authorisation letter delegating the registration to an unspecified assignee. The Great Court of Judicature held that such measure of transferring the certificate of shares was valid as commercial customary law. In one case, the assignor argued that the lack of procedure made the assignment invalid when the creditor of the assignee created a pledge over the share. The Court held that the assignor (plaintiff) who issued the authorisation letter to an unspecified assignee himself to transfer the share was bound by commercial customary law.[18] It may seem that the assignor in this case would be estopped from disputing the validity of the assignment, even if there were no customary commercial law. However, the principle of good faith, which is now considered to include estoppel, had not yet developed at the time of the decision.[19]

The Great Court of Judicature further held that such a practice of issuing an authorisation letter to an unspecified assignee validly transfers the share even if there is no accompanying share certificate, as long as the first assignor gave consent to delivering the share certificate upon demand from the last assignee.[20] The commercial customary law survived the amendments to the Commercial Code of 1938, which stipulated that a share

[17] Art.150, Commercial Code (prior to the 1938 amendments).
[18] Great Court of Judicature, 17 June 1902, *Minroku* vol 8, 94.
[19] See Luke Nottage, 'Tracing trajectories in contract law theory: Form in Anglo-New Zealand law, substance in Japan and the United States' (2013) 4 (2) *Yonsei Law Journal* 175, 211.
[20] Great Court of Judicature, 16 Oct 1919, *Minroku* vol 25, 1828.

certificate, whether named or unnamed, was transferred by means of endorsement.[21] The Great Court of Judicature reaffirmed the commercial customary law of transferring a share certificate by attaching an authorisation letter to an unspecified assignee in 1944.[22]

In another line of cases, the Great Court of Judicature held that a bill of exchange or a promissory note issued in blank (incomplete bill of exchange or incomplete promissory note), while not a valid instrument under the Act on Bills of Exchange and Promissory Notes, was a valid negotiable instrument under commercial customary law. Interestingly, earlier decisions simply held that an incomplete bill of exchange was valid under the Commercial Code (which then included the provisions on bills of exchange and promissory notes) by finding that it was the issuer's intention.[23] However, as the debates for the unification of the law on bills of exchange progressed, which later became the Geneva Convention, providing a Uniform Law for Bills of Exchange and Promissory Notes[24] adopted in 1930, the Great Court of Judicature started to refer to commercial customary law as the basis for incomplete instruments.[25] The shift in the case law coincides with the understanding that the Geneva Convention regards incomplete bills of exchange as valid under commercial customary law and included a provision on this subject.[26] The relevance of the Geneva Convention became all the more significant after Japan ratified and then implemented it by enacting the Act on Bills of Exchange and Promissory Notes in 1932. Here, the commercial customary law apparently reflected what was understood to be the global approach to the issue, rather than retaining the local practice against the foreign legal text.

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[21] Art.205, Commercial Code (after 1938 amendments until 1966 amendments).
[22] Great Court of Judicature, 29 February 1944, *Minshû* vol 23, 90. In the case at issue, however, the alleged right in the share was denied because the authorisation letter was not authentic; it had been forged.
[23] Great Court of Judicature, 27 December 1920, *Minroku* vol 26, 2109; Great Court of Judicature, 1 October 1921, *Minroku* vol 27, 1686.
[24] 143 *League of Nations Treaty Series* 257.
[25] Great Court of Judicature, 16 December 1926, *Minshû* vol 5, 841; Great Court of Judicature, 4 March 1930, *Minshû* vol 9, 233.
[26] See Mistuo Ôhashi, 1 *Shin Touitsu Tegata Houron* ('A Treatise on the New Uniform Law on Bills of Exchange and Promissory Notes') 148 (Yuhikaku 1932) (in Japanese).

Japan's highest court again affirmed commercial customary law in a case involving a reinsurance transaction.[27] When an insured accident occurs and the insurer indemnifies the insured, the insurer is subrogated to the right that the insured has against a third party pursuant to the provision in the insurance law (as codified in the Commercial Code at the time of the decision, now in Article 25 of the Insurance Act). While the same applies to the reinsurer having indemnified the original insurer, the Great Court of Judicature held that there is the customary law of 'loan form' by which the reinsurer consigns the original insurer to exercise the right on its behalf and forward the collected sum afterwards. In this case, the original insurance was on a ship damaged by a collision that occurred in Tokyo Bay. When the insurer of the original insurance raised a claim against the shipowner whose ship caused the collision in breach of the relevant navigation rules, the defendant advanced a defence that the original insurer could not exercise the right to which the reinsurer had already been subrogated. The Great Court of Judicature held that the original insurer was able to exercise the insured victim's right under its name according to the customary law of 'loan form' as described above and refused the defence of the owner of the guilty ship. Because the defendant in this case was a third party to the reinsurance transaction, customary law, as opposed to usage between the insurer and reinsurer, was relevant. This being said, apparently the real problem was the absence of an unambiguous contract in writing, a common problem in the global reinsurance market.[28]

So in the end, the commercial customary law found by the Great Court of Judicature was not law from a non-state source to fill the gap between the text of the Code and life in Japanese society. In the case of commercial custom concerning transfer of share certificate, the customary law responded to the needs of practice when the statutory requirements were too rigid and impractical. For incomplete negotiable instruments and loan form in reinsurance transactions, the commercial customary law had the role of introducing the globally accepted rules to Japanese commercial transactions. In both cases, the meaning of commercial customary law is not to endorse the parochial rules, which are different from

[27] Great Court of Judicature, 21 February 1940, *Minshû* vol 19, 273.
[28] Helmut Heiss, 'From Contract Certainty to Legal Certainty for Reinsurance Transactions: The Principles of Reinsurance Contract Law (PRICL)' (2018) 64 Scandinavian Studies of Law 91, 92-93.

the modern law codified in the national Codes, contrary to the assumption of the drafters of the Civil Code and *Hôrei*.

3.3 Cases referring to usage to interpret the contract

In contrast to the limited number of cases determining (commercial) customary law, there are many cases where the court has identified usage. Like the commercial customary law of 'loan form' in reinsurance markets, usage is used by the courts to clarify poorly drafted contracts. When the agreement between the parties to a dispute is not clear enough and can be read in more than one way, the court finds the usage and sides with one of the possible readings.

For example, in its decision of 2 November 1965, the Supreme Court affirmed the usage that a bank having discounted a promissory note from its customer was entitled to demand buy-back of the note by the customer when the latter became insolvent.[29] (Japanese companies widely use promissory notes, not bills of exchange, for payments of domestic transactions.)[30] The transactions between the bank and customer were based on the credit transaction agreement, which provided, amongst other things, that (i) when the bank discounts a promissory note from the customer, the customer owes a loan debt besides the obligation under the promissory note; (ii) all the debts and obligations of the customer become due when the customer defaults in payment or other signs of credit deterioration as specified occur; (iii) in the events listed under (ii), the customer admits that any claim that it may have against the bank, including a claim to demand repayment of a deposit, becomes suitable for setoff; and (iv) the setoff becomes effective from the time when the event under (ii) occurs. A week after the bank discounted a promissory note from the customer, the customer defaulted in payment, which the bank knew a month later. Against the bank's argument that the claim to demand repayment of the customer's deposit was

[29] Supreme Court, 2 Nov 1965, *Minshû* vol 19, no 8, 1927.
[30] Hirofumi Uchida, Arito Ono, Souichirou Kozuka, Makoto Hazama & Iichiro Uesugi, *Interfirm Relationships and trade Credit in Japan: Evidence from Micro-Data* (Springer 2015).

offset by the face value of the discounted promissory note, effective on the day the bank knew of the customer's default, the trustee of the customer now in bankruptcy argued that the offset was not valid under the Bankruptcy Act as it was an offset by a claim acquired after the creditor knew of the default of the debtor.

The Osaka Court of Appeal found that a bank discounting a promissory note acquires a claim to demand repurchase of the discounted note, either by explicit agreement or pursuant to custom as a fact (usage). The Court held that this is a conditional claim that arises from the time of discount and, therefore, is not excluded from setoff, as it exists before a customer is in default.[31] The Supreme Court upheld this finding of custom as a fact. That finding made up for the poor drafting of the credit transaction agreement, which was not clear about the bank's right with regard to the discounted promissory note. Japanese banks later amended the standard form for credit transaction agreements to explicitly provide for such a right to demand buy-back of the discounted note to eliminate the need for reliance on usage. The finding of usage in this case showed how a poorly drafted contract could be read, as well as suggested how the drafting could be improved.

Similarly, the District Court of Nagoya relied on usage to clarify the rights of two automobile insurers.[32] Under Japanese law, automobile insurance up to a certain amount is mandatory, and many automobile owners actually purchase *another* automobile insurance policy (so-called voluntary insurance) as a second tier of cover to increase the insured amount. The second tier insurance policy in this case provided that the insurer would indemnify the insured if the damages went beyond the amount payable by the mandatory insurance. Mandatory insurance was capped at 500 thousand yen at the time of the accident in issue. The insurer of the mandatory insurance assessed the damages incurred by the victim couple to be 82 thousand yen for the husband and 385 thousand yen for the wife and indemnified them in those amounts. The victims argued that they were in agreement with the insurer of the second tier (voluntary) insurance that the actual amounts of damages were 467 thousand yen for the husband and 461 thousand yen for the wife, and demanded the insurer indemnify the damages remaining after payment of the mandatory insurance.

[31] Osaka Court of Appeal, 11 April 1963, *Kôminshû* vol 16, no 4, 218.
[32] Nagoya District Court, 2 November 1973, *Hanrei Taimuzu* no 310, 245.

By refusing the argument of the second tier insurer that its responsibility was to indemnify only when the damages incurred were larger than the limitation amount of the first-tier insurance (ie 500 thousand yen), the court held that there existed the 'quasi commercial custom' (by which it may have meant usage) that the second tier insurer was to indemnify any difference between the amount of damages incurred and the amount actually indemnified by the first tier (mandatory) insurance. The defendant in the case was the Japanese subsidiary of a foreign insurance company, but the Court held that usage is binding on foreign insurers in Japan as well. Here again, the Court's finding of usage corrected the poorly drafted contract to ensure sufficient protection of the victims. As in the case of banks' credit transaction agreements, the insurers later amended the conditions of insurance and clarified that the second-tier insurer is responsible for indemnifying the damages above the amount actually indemnified by the first tier insurer.

Somewhat similarly, in a case decided by the District Court of Yokohama, the bank and the customer concluded an agreement for a current account, which included a provision 'The bank shall not be responsible for the payment of a lost, cheated, stolen or forged cheque when the bank examined the seal or signature of the cheque by comparing with the registered seal or signature'. The literal reading did not give a clear idea about the level of care that the bank had to exercise to be waived of its liability. The Court found that, according to the commercial custom in bank transactions in Japan, the bank having paid a forged cheque is waived of its liability, if the bank could not have discovered the forgery after having examined the cheque with due diligence, and held that 'the provision in the agreement together with the commercial custom' indicates the waiving of liability of the bank on condition that it exercised due diligence.[33] In this case, the bank was found to have exercised due diligence in paying the cheque forged by the employee of the customer. The Tokyo Court of Appeal upheld the decision.[34]

[33] Yokohama District Court, 4 March 1969, *Kin'yû Hômu Jijô* no 547, 26.
[34] Tokyo Court of Appeal, 28 November 1969, *Hanrei Jihô* no 577, 93.

In Japanese courts, usage is relied on not only to establish the rights and obligations of the parties in the absence of explicit contract clause, but also to clarify the meaning of a contractual term. As an example of this type of usage, the Great Court of Judicature held that the term 'on the rail of Shiogama' (in Japanese "*Shiogama Rêlu Ire*"), used in a contract for the sale of fertiliser (soybean meal) to specify the place of delivery, was equivalent to 'free on railway Shiogama', and that it implied the seller's obligation to dispatch the goods for Shiogama railway station in advance of the delivery date.[35] The dispute arose from the sale of fertiliser. According to the lower court's finding, the parties agreed that the delivery be made immediately, without specifying the delivery date. The lower court interpreted such an agreement to mean that the seller owed the duty to dispatch the fertiliser by railway service within a few days of conclusion of the sales contract. As the seller failed to do so, the lower court held that the buyer was entitled to terminate the contract. The Great Court of Judicature held that the lower court found and applied usage correctly.

In these cases, usage is used to clarify a contract that is poorly drafted. When the contract is not clearly written, a Japanese court tries to find out the true intent of the parties, as was argued in Terumichi's article mentioned above. Usage provides for a useful tool in this process. As in the case of commercial customary law, the function of usage in actual cases is not to fill the gap between the statutory text of foreign origin and real life in Japan. In other words, the drafters' view about the usage turned out to be invalid after the transplanted Western legal system matured in some decades. Then the courts have given the usage a different, still as important, role.

4. Procedural law and judicial control of usage

4.1 The customary law and usage as a real source

The shift in focus from customary law as a non-state legal source to custom as a fact (usage) to interpret a contract may, after all, best reflect the ideas of Ume among the three leading drafters of the Civil Code. After the Civil Code was implemented, Ume

[35] Great Court of Judicature, 2 June 1921, *Minroku* vol 27, 1038.

published a treatise of five volumes on the Civil Code and argued that Article 92 addressed custom as a fact (usage), as opposed to *Hôrei*, which addressed customary law.[36]

Customary law as a legal source is, procedurally, treated as foreign law. The relevant party must prove the existence and content of the customary law, and the court will enforce that law if the party is successful. The Great Court of Judicature affirmed that this is the rule under Japanese law by holding: 'when the appellant does not succeed in proving the existence of the custom, the court shall regard that the alleged custom does not exist, not needing to confirm the non-existence of the custom'.[37]

If customary law is equivalent to foreign law, the court's error in finding it (or failing to find it) would be a ground for appeal to the highest court. The same procedural treatment applies when usage is relied on to interpret the true intention of the parties under a poorly drafted contract. The Tokyo Court of Appeal so held in a dispute arising from the carriage of firewood by a barge. Against the consignee's claim to demand delivery of the goods, the Tokyo District Court affirmed the existence of custom as a fact (usage) that the carrier of firewood and charcoal on inland waters was not required to deliver the goods to the home of the consignee but was released of its obligation when it delivered the goods to a nearby berth and notified the consignee. The Tokyo Court of Appeal examined an expert witness and denied such a custom. Then the Court of Appeal (which was the highest court in the case) held that the error in applying custom as a fact (usage) amounted to an error in applying the 'empirical rules' (usual inference) in findings of facts (which can be a ground for appeal to the highest court under Japanese civil procedure law). The Court stated that the empirical rule is the general proposition deduced from numerous cases in practice and is not the issue of facts. The Court further elaborated:

> *'the laws and regulations do not always exhaust the creation, change and extinction of rights and obligations but are to be complemented by the*

[36] Kenjiro Ume, *Minpô Yôgi* ('A treatise on the Civil Code'), (revised 33rd edition first published 1911, Yuhikau 1984) 204.
[37] Great Court of Judicature, 26 October 1926, 15 *Hôritsu Gakusetsu Hanrei Hyôron Zenshû*, Civil Code 929.

empirical rules where the laws and regulations do not exist; furthermore, they are based on the empirical rules where they do exist. As a result, when interpreting the laws and regulations the court must be based on the empirical rules and the court ends up in derogating from the laws and regulations if it makes a finding against the empirical rules'.[38]

4.2 The judicial control of the customary law and usage

Customary law and custom as a fact (usage) are not treated in the exactly same manner as foreign law. In fact, Japanese courts tend to examine the reasonableness of a usage. This would never be the case if a finding of custom were equivalent to a finding of foreign law.

An example can be found in a case in which the director of a film claimed additional reward against the film making company when the home video edition of the film was published.[39] The contract of compensation was not clear on this point. The director alleged that he was entitled to the additional reward as provided for in the agreement between the Directors Guild of Japan and the Motion Picture Producers Association of Japan.[40] However, the plaintiff was not a member of the Directors Guild of Japan at the time, nor was the defendant film making company a member of the Motion Picture Producers Association of Japan. The court concluded that the agreement was not found as usage binding on non-members in the industry and dismissed the plaintiff's claim. In so holding, the court pointed to the fact that the agreement had been criticised as unfairly advocating the interests of the film directors to the disadvantage of other stakeholders in the film.

This case may be compared with the earlier decision of the Tokyo District Court, which affirmed a usage relating to the manuscript fee payable to a novelist.[41] According to the usage found by the court, that fee is to be determined pursuant to the novelist's popularity, with the payment to be made upon delivery of the manuscript if the novelist is

[38] Tokyo Court of Appeal, 16 November 1912, *Hôristu Shinbun*, no 846, 23.
[39] Tokyo District Court, 31 July 1995, *Hanrei Jihô* no 1543, 161.
[40] According to the director, the additional reward was to be calculated by multiplying 1.75 percent of the video's retail price by the number of videos sold, discounted by 0.2 percent.
[41] Tokyo District Court, 17 February 1950, *Kaminshû* vol 1, no 2, .229.

famous, or after a decision is made to publish the manuscript where the novelist is not so famous. The decision is very brief, in the style of 1950s Japanese judgments, and does not elaborate on the reasoning. However, the usage found by the court makes sense. If a novelist is popular, a publisher will not hesitate to publish his/her manuscript, and will pay for it pursuant to the 'market price'. Where the novelist is less popular, however, the publisher will be more hesitant and subject the manuscript to greater scrutiny before deciding on publication.

The court will even enforce a usage apparently contrary to globally accepted uniform rules as long as the court finds the relevant (local) usage to be reasonable. In a case concerning the letter of credit transactions, the Osaka District Court found a usage that the negotiating bank, having had the shipping documents and the bill of exchange renegotiated by another bank, needed to buy them back upon the request of the renegotiating bank.[42] In the background lay the practice in Japan that the bank negotiates the shipping documents and bill of exchange from the beneficiary of a letter of credit only on the basis of a foreign exchange transaction agreement, which provides for the bank's right to demand buy-back of the bill of exchange without requiring any justifiable reason.[43] As the standard form is widely used for foreign exchange transaction agreements, it is hardly possible to exclude such bank's right to demand buy-back. When a bank designated as a negotiating bank under the letter of credit has no foreign exchange transaction agreement with the beneficiary, the Japanese practice is for the beneficiary to ask its usual bank to negotiate the shipping documents together with the bill of exchange issued under the letter of credit. Then that bank (as a kind of agent of the beneficiary) requests renegotiation of shipping documents and the bill of exchange to the negotiating bank.

Under such a practice, the promise to 'buy-back upon request', equivalent to a provision included in a foreign exchange transaction agreement between the bank and its

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[42] Osaka District Court, 8 February 1990, *Hanrei Jihô* no 1351, 144. On this issue, see Souichirou Kozuka, 'Uniform Rules versus Freedom of Contract: Japanese Practice in Letters of Credit Transactions' (2000) 4(1) *Singapore Journal of International & Comparative Law* 148.

[43] It is obvious that the foreign exchange transactions agreement used here was inspired by the domestic bank-customer agreement, amended after the Supreme Court decision of 1965, mentioned above (n 29).

customer, applies when the renegotiation of the shipping documents and bill of exchange takes place between two Japanese banks. This is despite the fact that there is no written agreement for inter-bank transactions, as opposed to the bank-customer relationship. However, the dispute in the case before the Osaka District Court arose between two non-Japanese banks' branches in Japan. The negotiating bank refused the demand of buy-back by the renegotiating bank, arguing that such a demand ran counter to the principle of independence (abstract obligation) under letter of credit transactions.[44] The court found the right of the renegotiating bank to demand buy-back as usage and held that it was binding also on non-Japanese banks' branches in Japan. In its decision, the court followed the view of the expert witness, according to which such usage enables renegotiation to take place speedily without going through strict examination of the shipping documents, because the renegotiating bank can rely on the buy-back by the negotiating bank in case the issuing bank refuses indemnification under the letter of credit. The court then found that the plaintiff used the Japanese standard form agreement when it negotiated the shipping documents and bill of exchange from the beneficiary and that the agreement included a clause to demand buy-back without requesting any justifiable reason. According to the court, this fact proved that the plaintiff bank's branch in Japan also found the practice of buy-back useful. The negotiating bank as the plaintiff could not then deny the usage of buy-back on their side vis-à-vis the renegotiating bank. It is noteworthy that the court was not satisfied merely with a finding as to the existence of a usage; that usage also had to be reasonable.

In Japan, the reasonableness of a usage is not explicitly required in the Civil Code, but has emerged from the case law. The reason may be that Japanese courts treat a usage more as a kind of empirical rule (usual inference; translation of the German concept *Erfahrungssatz*) in identifying what the parties have truly intended, rather than as an independent source of a legal norm. In fact, judicial control of a usage by examining its reasonableness is not a universal idea. For example, the CISG includes no regulation of the

[44] The principle of independence is stipulated in Article 4 of the Uniform Customs and Practice for Documentary credits, 2007 revision (UCP 600).

content of a usage.[45] Still, the requirement of reasonableness does exist in the Unidroit Principles of International Commercial Contracts, Article 1.9, as well as in the PECL, Article 1:105, and the DCFR, Article II.-1:104. The latter two instruments admit the binding force of a usage in the absence of the agreement of the parties 'except where application of such usage would be unreasonable.' Notes to the PECL and DCFR mention that the requirement of reasonableness is not uncommon among the national laws of Europe.[46]

In today's society, trust in the judicial system at least in part depends on courts' moderate control of commercial practices. This may especially be the case where the transition to a market economy and the emergence (or resurgence) of emphasis on private law have been rather recent. Even if one may applaud legal pluralism through emphasis on private autonomy, national courts, as well as transnational tribunals, are required to subject such autonomous laws to the moderate control of reasonableness. Furthermore, the significance of judicial control of practice is not limited to the issue of custom and usage. The Civil Code of Japan after the reform of 2017 mentions the 'common sense in trade' (*torihiki jô no shakai tsûnen*) in various provisions, with regards to issues of control of standard contracts, finding of default that results in damages as well as conditions for cancellation, among others.[47] The moderate judicial control over practice has taken root in Japanese law after experiences over the last century. This will be a good model to the courts and tribunals struggling to establish people's trust in the judiciary.

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[45] See Ingeborg Schwenzer (ed), *Schlechtriem & Schwenzer Commentary on the UN Convention on the International Sale of Goods (CISG)*, (4th edn, OUP 2016) 183, Art 9, para 5 (by Schmidt-Kesel).
[46] Note 4(c) to Article 1:105, PECL: Note 20 to Article II.-1:104, DCFR.
[47] Artt.415, 541, 548-2, Civil Code. See Hiroo Sono, Luke Nottage, Andrew Pardieck and Kenji Saegusa, *Contract Law in Japan* (Wolters Kluwer 2019) 89, 148, 153. On the background thoughts, Souichirou Kozuka & Luke Nottage, 'Policy and Politics I Contract Law Reform in Japan' in Maurice Adams and Dirk Heirbaut (eds), *The Method and Culture of Comparative Law: Essays in Honour of Mark van Hoecke* (Hart, 2014) 235.

5. Conclusion and remaining issues

Japan has not had an easy experience with custom. The texts of the Civil Code and *Hôrei* were not unambiguous due to the lack of consensus amongst the drafters. And it is not surprising that the status of custom differed from that in Europe, given that the Civil Code was transplanted into the completely different social context of Japan. Furthermore, the reception of foreign academic thought after the implementation of the Japanese Civil Code has only led to more debate on the issue of custom.

Still, at least as far as commercial transactions are concerned, there was only limited room for customary law to serve as the legal source parallel to the national Codes and statutes. Instead, the courts have more often referred to custom as a fact (usage) in interpreting contracts, especially where those contracts have not been clearly drafted. Because the focus is not on the finding of a non-state law but on the interpretation of a contract, Japanese courts examine the custom's reasonableness before giving effect to it. With some linguistic complications due to the use of the same word '*kanshû*' for both custom and usage in Japanese, the courts have adopted an approach more or less equivalent to that now common in Europe, namely to consider usage in interpreting a contract to a not unreasonable extent. It is also noted that the moderate judicial control in Japan has now appeared in the texts of the Civil Code after the reform of 2017.

The issue that remains is how to determine reasonableness in actual cases. On one hand, the inconsistency among judges as to the standard of reasonableness would make dealing with this issue especially difficult. For this problem, the continuing training of judges could ensure a sharing of views and approaches among judges, and thus more consistency. In Japan, it is conducted through the seminars, lectures and group debates offered for judges by the Japanese Legal Research and Training Institute (an organ adjunct to the Supreme Court).[48] On the other hand, the recent emergence of services using new technologies, from social networking services (SNS) and smartphone apps to digital platforms and distributed ledger systems, endangers this approach of moderate judicial

[48] On the role of the Legal Training and Research Institute, see Souichirou Kozuka, '"Closing the Gap" between Legal Education and Courtroom Practice in Japan: *Yôken Jijitsu* Teaching and the Role of the Judiciary' in Andrew Harding, Jiaxiang Hu and Maartje de Visser (eds), *Legal Education in Asia: From Imitation to Innovation* (Brill, 2016) 157.

control over reasonableness. It is because the digital technology often formulates the users' rights through the technological architecture and not contracts. Yeung, taking up distributed ledger technologies (blockchain), points out the conundrum between respecting the individual freedom and autonomy and commitment to the rule of law,[49] which sound almost identical to the fundamental issue relating to the admission of customary law under the national legal system as it was discussed in the 'Introduction' above. While Yeung is optimistic about ensuring the supremacy of law where necessary, others, such as Hildebrandt, remain more sceptical about the possibility of digital codes (technological architecture) replacing the conventional text-written law.[50] The court finds it difficult to control the technological architecture as such. Both of these issues, however, are too complex to be properly discussed in this article and so are left for consideration in future studies.

[49] Karen Yeung, 'Regulation by Blockchain: The Emerging Battle for Supremacy between the Code *of* Law and Code *as* Law' (2019) 82 (2) *Modern Law Review* 207, 231.
[50] Mireille Hildebrandt, 'Code-driven law: Freezing the Future and Scaling the Past' in Simon Deakin and Christopher Markou (eds), *Is Law Computable? Critical Perspectives on Law and Artificial Intelligence* (Hart 2020) 67.