WHY SHAREHOLDERS SUE: 
THE EVIDENCE FROM JAPAN 
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PAPER #00-010 

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Why Shareholders Sue: The Evidence From Japan

Mark D. West*

ABSTRACT

This Article explores the dynamics of and motivations behind shareholder litigation in a heretofore overlooked context: Japan. Following a 1993 reduction of filing fees, the number of shareholder derivative suits filed in Japan has increased dramatically, creating a database from which to study litigation incentives. This Article shows that most plaintiffs in Japan lose, few suits settle, settlement amounts are low, and, as in the United States, shareholders do not receive direct stock price benefits from suits. Most derivative suits in Japan, as in the United States, can be explained not by direct benefits to plaintiffs, but by attorney incentives.

But derivative suits, like most things in life, have more than one source of causation. The residuum of suits not explained by attorney incentives is best explained by a combination of (a) non-monetary factors such as altruism, spite, and social concerns, (b) corporate troublemakers (sokaiya), (c) insurance, and (d) close corporation fights. I also find that many derivative actions “piggyback” on government enforcement actions in Japan, which, especially given the lack of information available to shareholders and low white-collar crime enforcement rates, raises interesting questions regarding the relationship of public and private enforcement. These findings suggest that the difficult and messy issues of derivative suits are not unique to the relatively “litigious” or “attorney-centered” United States, and instead simply are endemic to the derivative suit mechanism.

* Assistant Professor of Law, University of Michigan Law School. For their comments on early drafts, I thank Merritt Fox, Koichi Hamada, Rick Lempert, Ronald Mann, Curtis Milhaupt, Adam Pritchard, Mark Ramseyer, Roberta Romano, and participants at workshops at Michigan and Yale. I also thank Eric Smith and Nancy Vettorello for excellent research assistance. Opinions and errors are of course mine. I conducted twenty formal and numerous informal interviews for this project; those that are unsourced were conducted on the condition of anonymity. This Article was funded by the Nippon Life Insurance Company’s endowment at the University of Michigan Law School.
INTRODUCTION

Why do shareholders sue? In the United States, the story is well known. Shareholders seldom profit – suits are filed because their attorneys stand to reap substantial fees. Legal scholars have written extensively about this incentive structure, and even offered a few theoretical solutions for reform. In this Article, I examine litigation incentives in a different, heretofore overlooked context. I look closely at derivative suits in Japan, an institutional environment in which attorneys fees are lower than in the United States, and which has seen a recent dramatic rise in derivative litigation in recent years.

Shareholders in Japan filed fewer than twenty derivative suits against directors from 1950 to 1990, while nearly one-fifth of a random sample of publicly traded U.S. corporations saw such suits during a similar period. In an article I wrote eight years ago, I argued that Japanese shareholders had chosen not to sue not because of cultural mores, but because of high filing fees, high attorneys’ fees, corporate governance constraints, and comparatively low incentives for Japanese attorneys. Still, I noted that a 1993 legislative reduction of filing fees had brought about an “explosion” in Japanese derivative litigation – about twenty suits were pending in the Tokyo District Court in 1993 as the article went to press -- and predicted that more suits would follow.

My unwritten inclination at the time was that derivative litigation would increase to about ten cases per year. But by the end of 1993, 84 suits were pending in Japanese courts. By 1996,
that number rose to 174, and by the end of 1999, there were 286 such suits, including 95 filed in 1999 alone.\(^4\) The huge increase in suits – over 10,000\% -- has prompted calls by business for legislative reform, led to new corporate governance innovations, and sparked a general public debate of the proper role of shareholders and directors in Japanese corporate governance.

The loudest calls for reform followed a September 2000 judgment by the Osaka District Court against 11 directors of Daiwa Bank. In September 1995, it was revealed that a trader in Daiwa’s New York branch had lost $1.1 billion through eleven years of illegal trading of U.S. Treasury bonds. A shareholder and former Bank employee subsequently filed suit. The Osaka court, citing the directors’ failure to establish a monitoring system, found violations of the directors’ duties of care and loyalty and ordered them to pay a whopping U.S. $775 million to the company.\(^5\) The amount of damages (66 times higher than the previous record award) and the basing of liability on “mere” failure to monitor shocked the Japanese business and legal community to an extent that invites comparison to *Smith v. Van Gorkom*.\(^6\) The comparison was made even more appropriate by the fact that the directors’ insurance policy did not cover the period in which the violations occurred, and even if it had, it would not have covered the full amount of damages. Much like the Delaware reaction to *Van Gorkom*, a flurry of activity followed, as both sides appealed, legislators searched for legal fixes, insurance companies sold large new policies, editorials criticized, and companies sought legal advice.

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\(^5\) Nishimura v. Yasui, Osaka District Court, 199 SHIRYÔBAN SHJ MUS 264 (Judgment of Sept, 20, 2000). The court found the New York branch manager at the time the trading occurred liable for $530 million of the $775 million total.

\(^6\) 488 A.2d 858 (Del. 1985).
In my earlier work, I attempted to explain why Japanese shareholders did not sue. In this Article, in addition to the basic goal of exploring the functioning Japanese derivative suit mechanism, I attempt to explain why they do, a question that was virtually impossible to answer until the 1993 reforms created a dataset of cases. This Article is based on my review of a dataset of 140 cases filed between 1993 and 1999 and subsequent developments in these cases through 2000.

The 1993 lowering of filing fees from a percentage of requested damages to a flat ¥ 8,200 (about $75) explains much of the increase in cases filed. Lower the cost of suing, and more people will sue. The post-Bubble decline in the Japanese economy may also influence some cases, as plaintiffs may find it easier to prove damages against flailing firms.

But the number of suits is nevertheless intriguing given the continuing lack of shareholder incentives to sue. Attorneys’ fees, which drive U.S. derivative litigation, have changed little in Japan. Because damages in derivative suits in Japan, as in the U.S., are paid to the corporation, the most a plaintiff can hope for is a pro rata increase in the value of her individual stake. In Japan, as this Article will show, plaintiff-shareholders usually lose. And filing fees, though reduced, are still nonzero. Why should a plaintiff pay $75, or even $1, for a losing case? Shareholder-plaintiffs in Japan are undertaking costly activity – lawsuits – despite minimal evident benefits, in apparent contradiction with economic theory.

Japan presents a particularly good comparative model from which to explore these issues. Besides the fact that the derivative suit mechanism was transplanted directly from the U.S. model in 1950, the simplicity of the Japanese case controls some extraneous variables that drive litigation in the United States. Because Japan has no class action mechanism, derivative suits
account for almost all shareholder litigation. Because derivative suits may be brought only against directors and similar actors, there are no confounding variables of suits brought against outside third parties. The Japanese system also comes with relatively little historical baggage and path-dependent legal outcomes. Due to a scarcity of derivative litigation before 1993, Japan lacks consistent and thorough legal doctrine in many of the areas affected by such litigation. The Japanese experience may thus offer useful insights for both developed and developing economies considering various approaches to shareholder rights, enforcement of directorial duties, and related corporate governance questions.

In this Article, I make three claims. First, derivative litigation does not appear to increase shareholder wealth directly. Japanese shareholders rarely win, and, unlike their counterparts in the United States, they only occasionally obtain settlement. Nor do they receive stock-price gains. Importantly, I test for these gains to shareholders using the same event study methodology used in other studies to test gains from derivative actions in the United States. One advantage of this approach is that it allows for an examination of whether those studies – and mine – are biased by peculiarly national institutions, culture, or other nation-specific factors. The similarity of results suggests that such biases are minimal at best.

Second, while popular and academic critics sometimes blame U.S. derivative litigation on a peculiarly American excess of overpaid attorneys and litigious norms,8 I find the same basic jumbled set of attorney and plaintiff incentives at work in Japan. Multiple causation and multiple motivations are of course at work on both attorneys and plaintiffs in both countries, and

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most players have some combination of monetary and non-monetary incentives. But in general, even with lower attorneys’ fees, attorneys are the driving force behind Japanese derivative litigation. A residuum of suits can be explained by an amalgam of (a) non-monetary factors such as altruism, anger, and social concerns both among attorneys and plaintiffs, (b) corporate troublemakers, (c) insurance, and (d) close corporation fights. The Japanese experience suggests that the difficult issues of attorney incentives are endemic not to the United States in particular, but to the derivative suit mechanism in general.

Third, the Japanese mechanism may differ in one important respect: its place in the overall enforcement scheme. The Japanese civil, criminal, and social schemes for enforcing directors’ duties appear relatively weak in comparison with those of the United States. Although the evidence is far from clear, in light of weak overall enforcement, the provision of a civil disgorgement remedy in the form of derivative litigation in Japan may lead to systemic benefits not seen in the United States.

Before proceeding, it is important to note that my focus here is large, public corporations. Such firms are the usual focus of analysis, are the primary subject of analysis in the media, and generally provide much more data than smaller firms. In fact, the event study analysis that I conduct in Part II is only possible with such a focus. Still, I recognize that the study of other firms could be probative, and I address those issues in Part III.

The Article proceeds as follows. In Part I, I briefly sketch the background of Japanese shareholder suits and compare them to their counterparts in the United States. In Part II, by examining success rates and using simple econometric tests, I examine whether shareholders in Japan benefit directly from derivative litigation. Part III discusses attorney incentives and a residuum of non-monetary factors, corporate troublemakers, insurance, and close corporation
fights. Part IV explores the complex relation between public and private enforcement of director wrongdoing.

I. DERIVATIVE SUIT MECHANICS

Because I have discussed the mechanics of Japanese derivative suits elsewhere in detail, here I only outline the basics. In Japan as in the United States, a shareholder may bring suit on behalf of the corporation against a director to enforce a director’s duties to the corporation. The shareholder’s right to sue “derives from” her shareholding, and any damages paid by the defendant are paid not to the shareholder, but to the corporation.

The similarities between Japan and the United States are great, but differences can be found in the details. In the United States, derivative suits may be brought against any third party; in Japan, they may only be brought against directors and other similarly situated parties. While most U.S. regimes have a contemporaneous ownership requirement, Japan requires only that a shareholder have held shares continuously for six months before bringing suit. In contrast to Delaware’s complicated demand rules, Japan, like the American Law Institute, requires universal demand.

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9 West, supra note 2, at 1444-56.
10 For Delaware, see Grobow v. Perot, 539 A.2d 180 (Del. 1988); for Japan, Sh unh art. 196; see also West, supra note 2, at 1446-47.
11 Sh unh art. 267(1).
12 See, e.g., Grimes v. Donald, 673 A.2d 1207 (Del. 1996)(Delaware); AMERICAN LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 7.03 (ALI); Sh unh art. 267 (Japan).
When a Japanese case reaches the courtroom, the first crucial decision is the court’s judgment of whether to require a plaintiff to post a bond.\(^{13}\) The Commercial Code (arts. 267(6), 106(2)) requires a defendant seeking to force a plaintiff to post bond to satisfy the court that the plaintiff brought the suit in bad faith. The dominant view expressed by the Tokyo District Court is that “bad faith” includes cases in which the plaintiffs brought suit with little hope of success, or that would likely be dismissed by defendants.\(^{14}\) Of the fifteen post-1993 cases that I found in which the court ordered plaintiffs to post bond, the average requirement was ¥ 162 million, or about $1.5 million. In two of those cases, plaintiffs withdrew their suit, in seven the defendants won (either on the merits or because plaintiffs failed to post bond), one settled, and seven remain pending.

In Japan the loser pays court costs.\(^ {15}\) If a plaintiff wins, because the damages accrue to the company, the Commercial Code (art. 268-2) provides that the company shall pay a “reasonable amount” of attorneys’ fees upon plaintiff’s motion. Defendants pay their own attorneys’ fees.

Before 1993, the biggest roadblock to shareholder litigation was the requirement that plaintiffs pay a litigation fee in the form of revenue stamps that must be attached to the

\(^{13}\) Shih\(^{\text{art. } 267(5)}\). Most U.S. jurisdictions have followed the MBCA and eliminated the requirement. On the merits of the system, see Note, Security for Expenses in Shareholders’ Derivative Suits: 23 Years’ Experience, 4 COLUM. J.L. & SOC. PROBS. 50 (1968).

\(^{14}\) Suzuki v. Yasuda (Janome Machine Case), Tokyo District Court, 1504 Hanrei Jiho 121 (Jul. 22, 1994); cf. Suzuki v. It\(^{\text{Tokai Bank case}}\), Nagoya District Court, 119 Shiry\(^{\text{Shoji H\mu 188}}\) (Jan. 26, 1994)(finding no bad faith despite plaintiff’s sokaiya history), rev’d, Nagoya High Court, 1531 Hanrei Jiho 134 (Mar. 8, 1995); see also Hideyuki Koboyashi, Daihy\(^{\text{Sosh\niOkeru Tanpo Teiky\to Genkoku no Akui [Derivative Suit Bond Requests and Plaintiffs’ Bad Faith], 47 JY\_\to SEIGI 113 (1996) (survey).}}

\(^{15}\) Minsoh\(^{\text{art. 89}}\). A plaintiff may also be liable for tort damages if he brings a claim knowing that there is in fact no liability. Minp\(^{709}\); See UTTAERU GAWA NO KABUNUSHI DAHY\=SOSH\=79 (Nikk\=Sh\=ken Bengodan ed. 1994).
complaint. The amount required was based on a sliding scale relative to the amount of damages claimed; for instance, about $25,000 for a $10 million claim against management.

Before 1993, there was academic debate regarding the proper amount of litigation fees required for a derivative suit.\(^\text{16}\) Most argued that the courts were right; fees should be determined by the sliding scale. But some scholars argued that because the amount of damages to be paid to the suing shareholder (not the corporation) was indeterminate, the fee should be fixed at ¥ 8,200 (about $75), in accordance with a procedural rule that set damages at ¥ 950,000 in such cases.\(^\text{17}\) In the 1993 *Nikkû Securities Case*,\(^\text{18}\) the Tokyo High Court agreed with this logic, saving the plaintiff-shareholders approximately $2 million in fees. Several months later, following the Tokyo High Court’s logic, the Diet revised the Commercial Code to lower the filing fee for all derivative actions to ¥ 8,200. It is this Commercial Code revision that marks the watershed in Japanese shareholder derivative litigation. As Table 1 shows, following the 1993 revisions, derivative litigation rates increased dramatically.

<table>
<thead>
<tr>
<th>Year</th>
<th>Pending, District Court</th>
<th>Pending, High Court</th>
<th>Total Pending</th>
<th>New Cases, District Court</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>74</td>
<td>10</td>
<td>84</td>
<td>Not available</td>
</tr>
<tr>
<td>1994</td>
<td>133</td>
<td>12</td>
<td>145</td>
<td>Not available</td>
</tr>
<tr>
<td>1995</td>
<td>158</td>
<td>16</td>
<td>174</td>
<td>Not available</td>
</tr>
<tr>
<td>1996</td>
<td>174</td>
<td>14</td>
<td>188</td>
<td>71</td>
</tr>
<tr>
<td>1997</td>
<td>203</td>
<td>16</td>
<td>219</td>
<td>83</td>
</tr>
<tr>
<td>1998</td>
<td>222</td>
<td>18</td>
<td>240</td>
<td>68</td>
</tr>
<tr>
<td>1999</td>
<td>258</td>
<td>28</td>
<td>286</td>
<td>95</td>
</tr>
</tbody>
</table>


\(^{17}\) See, e.g., AKIRA KAWATANI, MINJI SOSHû Yû INSHI NO KENKYû [A STUDY OF CIVIL LITIGATION REVENUE STAMPS] 78 (1962). The relevant law is Minji Soshû Hû Yû Tî ni Kansuru Hûritsu [Law Concerning Civil Litigation Costs], Law No. 40 of 1974, Art. 4(2).

\(^{18}\) Asai v. Iwasaki, Tokyo District Court, 797 Hanrei Times 382 (Aug. 11, 1992), rev’d, Tokyo High Court, 823 Hanrei Times 131 (Mar. 30, 1993).
Corporate Japan was generally not thrilled with the increase in derivative litigation. Although plaintiffs and shareholder activists (and for the most part, the media) proclaimed a new age of corporate governance in which managers were responsible to shareholders, many managers complained that the suits were nuisance suits of groundless claims looking for cheap settlement.

Nuisance or not, change came. Corporations purchased D&O liability insurance policies. Legal departments in large companies suddenly wielded new clout. Lawyers invented new methods for giving managers power without putting them on the board, where they would risk liability.

Still, shareholder-plaintiffs face an uphill battle. Shareholders in Japan, as in the U.S., often lose because of the business judgment rule. Appropriately or not, Japanese courts, usually composed of career judges with no business experience, are especially reluctant to second-guess Largely in response to cries from the business community, the ruling Liberal Democratic Party in April 1999 released a draft Commercial Code reform plan. Jiyū Minshū Seimu Chōsaikai Hōmubukai Shōhō ni Kansuru Shoinkai, Kigyō Tōji ni Kansuru Shōhō ni Kansuru Yōkakusei [Outline of Commercial Code Revision Plan on Corporate Governance], 1524 Shōhō 37 (1999). Among other things, the plan called for limiting the ability of a shareholder who purchases shares knowing in advance of directorial misdeeds, allows a company to assist in defense of directors in derivative suits, and allows a limitation of liability of directors by shareholders to an amount equal to two years of the directors’ salary. The plan was quickly opposed by many observers, largely on the grounds that it is “one-sided and impatient.” Michiyo Hamada, Kigyō Ronri no Kakuritsu to Kansayaku, Daihyō Soshō Seido [The Establishment of Corporate Logic and the Auditing and Shareholder Derivative Suit Mechanisms], 1123 JURISUTO 114, 124 (1997); Kabunushi Daihyō Soshō Seido Kenkyū Kai, Jiminritsu no “Kigyō Tōji ni Kansuru Shōhō ni Kansuru Yōkakusei ni Taisuru Iken” [Opinion on the LDP’s “Outline of Commercial Code Revision Plan on Corporate Governance”], 1526 Shōhō 39 (1999). Although the plan was not adopted, some of its ideas, such as allowing a corporation to assist a defendant director, were adopted by courts, see Koya v. Kurosawa, Tokyo District Court, 1709 HANREI JIHO 3 (Apr. 25, 2000), and Daiwa may bring further changes.

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19 HIDEAKI KUBORI & NAOTO NAKAMURA, KABUNUSHI DAIHYO SOSHOU TO YAKUIN NO SEKININ [SHAREHOLDER DERIVATIVE SUITS AND OFFICER LIABILITY] 188 (1993)

the business judgment of directors. In the next Part, I examine more precisely plaintiff success rates and other benefits of suit.

II. DIRECT BENEFITS TO SHAREHOLDERS?

Perhaps the easiest way to determine whether benefits accrue to shareholders is to examine success rates in court. To do so, I examined a database of derivative suits filed between 1993 and 1999 and published in the legal journal Shiryōban Shōji Hōmu. This database contains 73 derivative suits and is the most comprehensive published database available. Of the 73 cases listed, only one case with a final verdict was an outright victory for plaintiffs. Only nine cases settled. Twenty cases were either decided for defendants or were withdrawn by the plaintiff in response to an adverse ruling. Forty-four cases are pending, and only three of those 44 pending cases are pending because of appeals by defendants of adverse judgments.

Still, despite this overall record, winning plaintiffs might profit from derivative suits. Although damages are paid to the corporation and not directly to shareholders, shareholders might receive direct economic benefits from derivative suits in the form of higher stock prices.

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21 In applying the business judgment rule, Japanese courts often blur the line between procedure and substance, see Hideki Kanda, Kabunushi Daihyō Soshū ni Kansuru Riron'eki Sokumen [The Theoretical Side of Shareholder Derivative Suits], 1038 JURIUSUTO 65, 68 (1994). In other cases, it appears that ignorance may exonerate. To take a recent well-publicized example, the Supreme Court held in July 2000 that while Nomura Securities directors had broken the law in paying a client 360 million yen ($3.6 million) in compensation for losses incurred by the client, shareholders were not entitled to compensation because management was not aware of the illegality of their actions. See Ihn, Ninshiki Nai [Not Aware of Illegality], ASAHI SHINBUN, July 8, 2000, at 37.

22 See chart, 192 SHIRYŌ BAN SHŌJI HŌMU 170 (2000). The Shōji Hōmu Kenkyū-kai (Commercial Law Center) has been so active in reporting derivative suits (including motion papers and minor decisions) in its main journals (Junkan Shōji Hōmu, Bessatsu Shōji Hōmu, and Shiryōban Shōji Hōmu) that it is far and away the most comprehensive database. The database is somewhat biased in that it lists only “important” cases, most of which involve large public companies, and important means “covered in trade publications or the mass media.” I know of no case against a Tokyo Stock Exchange firm that is not listed in the database. The Hanrei Taikei CD-Rom database, which contains only final opinions but is usually quite comprehensive, contains only thirty-one post-1993 shareholder derivative cases, and several of those were filed before the 1993 Commercial Code amendments took effect.
Only if prices rise can the compensatory goals of derivative litigation be realized. If derivative litigation raises stock prices sufficiently, plaintiffs might be willing to sue in order to sell their shares later at increased prices.

To examine the potential direct benefits from derivative suits, I conducted several experiments using a modified Shiryu ban Shoji Hana database. To measure stock price benefits, I narrowed down the 73 cases to the 56 cases filed against Tokyo Stock Exchange companies. Of these 56 cases, in two instances, different plaintiff groups filed suit against the same companies on the same date (IBJ and Nomura Securities). Three suits are against companies that have been delisted from the Tokyo Stock Exchange and as such do not have complete stock price data (two against Yamaichi Securities; one against Hokkaido Takushoku Bank). Removing these five suits leaves a total of fifty-one suits in the database.

I performed several empirical tests using this database. First, as Roberta Romano did in her seminal article on U.S. derivative litigation,²³ I used well-established event study methodology to measure the stock price effects of filing suit. In her event study of 66 derivative and class actions in the U.S., Romano found that the average abnormal return on the day a suit is filed is positive and borderline significant, while the abnormal return of the day before suit is filed is significantly negative. Splitting the sample into derivative suits and class actions

²³ Romano, supra note 2, at 65-66. Romano’s study, like most important works, is not without its critics. Melvin Eisenberg, for instance, notes that Romano’s study is incomplete in that it only measures immediate benefits to shareholders, ignoring deterrent effects and the ability of suits to shape legal rules. Melvin A. Eisenberg, Corporate Law and Social Norms, 99 Colum. L. Rev. 1253, 1276 (1999); see also Edward B. Rock, Saints and Sinners: How Does Delaware Corporate Law Work?, 44 UCLA L. Rev. 1009, 1097 (1997). John Coffee goes so far as to say that “any claim that the empirical data proves the derivative action useless is circular.” Quoted in MELVIN ARON EISENBERG, CORPORATIONS AND OTHER BUSINESS ORGANIZATIONS: CASES AND MATERIALS 1059 (8th ed. 2000). But these critiques, to the extent that they hold up, largely concern Romano’s conclusions, not her methods. Unlike Romano, I draw no conclusions on the merits of Japanese derivative litigation from event study data, as my primary goal is to examine litigation incentives.
revealed that “derivative claims produce no significant impact” on either the day of filing or the preceding day.\textsuperscript{24}

Table 2 shows the results of an event study of the stock price effects on the filing dates of the 51 Japanese firms.\textsuperscript{25} The results of my regressions of Japanese firms differ little from Romano’s study of U.S. firms: Japanese derivative suits do not result in statistically significant stock price movements. In some ways, this result is unsurprising, as moderate damage payments to a widely dispersed body of shareholders might not be expected to cause large price swings. But the lack of significant price adjustments (and in fact negative measures for all but one day) suggests a stronger claim: shareholders apparently do not expect to receive gains of any sort or magnitude from filing, whether from awards of damages, from future specific deterrence, or from lawsuit-induced restructuring of corporate governance mechanisms.

<table>
<thead>
<tr>
<th>Day or Event Window</th>
<th>Market-Adjusted Return</th>
<th>$z$</th>
<th>% Positive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Day before lawsuit filed</td>
<td>-.112%</td>
<td>-.032754</td>
<td>42.9</td>
</tr>
<tr>
<td>Day lawsuit filed</td>
<td>0.0597%</td>
<td>0.278872</td>
<td>44.6</td>
</tr>
<tr>
<td>Day after lawsuit filed</td>
<td>-.374%</td>
<td>-1.57994</td>
<td>39.3</td>
</tr>
<tr>
<td>Day of suit + day after</td>
<td>-.314%</td>
<td>-.91999</td>
<td>39.3</td>
</tr>
</tbody>
</table>

\textsuperscript{24} Romano, supra note 2, at 67. See also Sanjai Bhagat et al., The Shareholder Wealth Implications of Corporate Lawsuits, FIN. MANAGEMENT, Winter 1998, at 5 (finding negative returns on filing date when corporation is defendant, but not in corporate governance suits); Mark L. Cross et al., The Impact of Directors and Officers’ Liability Suits on Firm Value, 45 J. RISK & INS. 128 (1989) (finding negative impact on firm value from suit). Romano also examines the date on which the lawsuit filing is reported in the Wall Street Journal. In Japan, the filing of a derivative suit remains against a large company remains such a reportable event that it is almost always carried in the Nihon Keizai Shinbun, either in the evening edition the day of the filing, or the morning edition the next day, and very frequently appears on the national evening news.

\textsuperscript{25} I use standard event study methodology, with market model parameter estimates measured 240 days beginning 300 days before the event date. A two-day window is standard. See RONALD J. GILSON & BERNARD S. BLACK, THE LAW AND FINANCE OF CORPORATE ACQUISITIONS 204 (2d ed. 1995); Stephen J. Brown & Jerold B. Warner, Using Daily Stock Returns: The Case of Event Studies, 14 J. FIN. ECON. 3 (1985). On the efficiency of the Tokyo Stock Exchange, see, e.g., SHIGEKI SAKAKIBARA ET AL., THE JAPANESE STOCK MARKET: PRICING SYSTEMS AND ACCOUNTING INFORMATION (1988). I experimented with several other methodologies, including adding industry controls, adjusting the market model to include periods after the event window, and controlling for window variance. See generally Brad M. Barber & Lohn D. Lyon, Detecting Long-Run Abnormal Stock Returns: The Empirical Power and Specification of Test Statistics, 43 J. FIN. ECON. 341 (1997). Because results did not differ significantly in any case, I report here the results using the most common methodology.
In another important empirical study of derivative suits in the United States, Daniel Fischel and Michael Bradley examined the stock price reactions to management motions to dismiss derivative suits, composed of eighteen court-ordered terminations and six non-dismissals. Fischel and Bradley used event study data to make the claim that “neither termination nor continuation of a derivative stockholder suit has a significant effect on the wealth of the firm’s stockholders.”

Again, I conduct a similar event study for Japan to measure the stock price effect of judicial screening. In Japan, the relevant screening mechanism is not the dismissal motion, but the judicial decision of whether to require plaintiffs to post a bond. Because of the expense of posting bond and the nature of the “bad faith” standard, a requirement that the shareholder-plaintiff post a bond is similar to a dismissal in the United States for failure to state a claim upon which relief can be granted pursuant to rule 12(b)(6). My sample contains 13 separate event dates (for 15 companies; in two cases the court ruled on two bond motions on the same day) in which the court ruled that plaintiffs were required to post bond and four cases in which the court denied management’s motion to require the posting of bond. Table 3 shows the results of an event study on bond-required cases. I include the bond-denied cases only for reference; the sample size is too small to draw any meaningful inferences.

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The results of decisions not to require plaintiff to post bond have no statistically
significant impact. But the results of the bond-required cases are intriguing. Although the day
after the court’s decision appears to have little impact, the day of the court’s decision is
significantly positive. In contrast to Bradley and Fischel’s results, my calculations thus
tentatively suggest that a small increase in shareholder wealth occurs when Japanese courts
require plaintiffs to post bond. These results, admittedly based on a small sample, are difficult to
interpret. Perhaps the market believes that the suits are nuisance suits, and is pleased to be rid of
them.27 Or perhaps given the “bad faith” standard, the market believes that the requiring of a
bond is equal to a finding of no liability. Finally, given that the returns are positive on the day of
the court decision for the tiny sample of non-dismissal cases, perhaps the market is simply
reacting to any news regarding the case, regardless of the disposition.28

Finally, I looked at final dispositions of cases. Of the fifty-one cases in the sample of
Tokyo Stock Exchange firms, twenty-five cases are pending, and only two of those cases are

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Footnotes:
27 I also tested the effects of filing a suit on the bond-required and bond-not-required subgroups, in an attempt to
see whether stockholders could judge ex ante the legal validity of a suit. See A.C. Pritchard & Stephen P. Ferris,
Stock Market Effects of Securities Fraud Class Actions Under the Private Securities Litigation Reform Act,
unpublished manuscript. In neither case did I obtain significant results.

28 An added complication is the fact that investors must receive word of negative rulings on bond motions from
sources other than large news organizations. Although I found references to three of the four rulings in minor trade
publications and financial newspapers, I found no such reference in the mainstream press.
defendants’ appeals. Seventeen cases were decided for defendants. Although an examination of the stock price effects of awards to plaintiffs might be probative, only two firms in the sample, the Hazama political bribery case\textsuperscript{29} and the Daiwa Bank illegal trading case (now on appeal) fit such criteria.\textsuperscript{30} The two-day return in both cases individually and combined was insignificant,\textsuperscript{31} but the sample size alone is notable: in only two cases in the entire Tokyo Stock Exchange sample did plaintiffs win, and one of those is on appeal. Like their U.S. counterparts, the success rate for shareholder-plaintiffs in court in Japan is, in a word, abysmal.

Because of the lack of final judicial dispositions, I focus on settlements. Only nine firms in the Tokyo Stock Exchange sample reported settlements. Although some cases surely settle quietly, no other cases in the Tokyo Stock Exchange sample were withdrawn in the absence of an adverse judicial ruling, suggesting that settlement truly is rare, at least in suits against directors of large companies. Again, this fact alone is significant. While most suits in the U.S. settle,\textsuperscript{32} most suits in Japan apparently recover nothing. Although many factors can explain the difference (including that most suits are frivolous), one explanation might be that Japanese

\textsuperscript{29} Matsumura v. Otsuru (The Hazama Case), Tokyo District Court, 130 SHIRY\textsuperscript{BAN SHIJI H\textsuperscript{MU} 94 (Dec. 22, 1994).

\textsuperscript{30} One additional case filed one year before the 1993 law took effect (and as such not included in the sample) but decided in 1996 was also a winner: plaintiffs in the Japan Aviation Electronics Industry Ltd. case were awarded ¥1.24 billion (about $12.4 million) by the Tokyo District Court, and eventually settled for ¥100 million ($1 million) in 1997. I found no significant stock price effects on either event date.

\textsuperscript{31} Interestingly, the stock price effects of the Osaka District Court’s decision in the Daiwa Bank case were positive and marginally significant on the day of the decision (2.0938%, $t = 1.739) and significantly negative the following day (-2.465%, $t = -2.198$). This phenomenon is perhaps best attributed to the content of news reports: \textit{Nihon Keizai Shinbun} coverage the day of the verdict merely mentioned the plaintiffs’ victory, \textit{Daiwagin Kyogaku Sonshitsu, Moto Yakuinra ni 820 Oku en Baish \textsuperscript{Meirei}, [Former Executives Ordered to Pay ¥ 82 Million over Daiwa Bank Massive Loss]}, \textit{NIHON KEIZAI SHINBUN}, Sept. 20, 2000 (evening edition), at 1, while the same influential newspaper the following day reported that the because the events predated the directors’ D&O insurance coverage, plaintiffs were unlikely to recover the full amount. \textit{Daiwagin Kabunushi Daihy\textsuperscript{Sosh}, Chisai Hanketsu, [District Court Judgment in Daiwa Bank Derivative Suit]}, \textit{NIHON KEIZAI SHINBUN}, Sept. 21, 2000, at 3.

\textsuperscript{32} Romano, \textit{supra} note 2, at 60; see also Thomas M. Jones, \textit{An Empirical Examination of the Resolution of Shareholder Derivative and Class Action Lawsuits}, 60 BOSTON U. L. REV. 542, 422 (1980) (most suits result in some recovery for shareholders).
defendants are better able than U.S. defendants to determine that the expected value to plaintiffs of going to trial is negative,\textsuperscript{33} for at least four reasons. First, Japanese courts side with plaintiffs with relative infrequency. Second, the lack of a discovery mechanism creates informational asymmetries in which defendants know much more about the facts than plaintiffs. Third, although the \textit{efficiency} of the Japanese “loser pays” rule is unclear, it at least strengthens the bargaining power of defendants. Finally, the lack of an extensive body of derivative suit caselaw in Japan may reduce the ability to enter into a settlement in the shadow of the law.

Of the nine settling firms in the sample, I was unable to find a settlement amount for one firm, and removed it. Before examining the stock price effects, it is useful to compare settlement amounts and awards per share. Table 4 shows the average amounts per outstanding share that in theory should be gained from a settlement in each case, absent transaction costs.

<table>
<thead>
<tr>
<th>Company</th>
<th>Issue</th>
<th>Damages Claimed</th>
<th>Settlement Amount</th>
<th>Settlement amount per share$\textsuperscript{a}</th>
</tr>
</thead>
<tbody>
<tr>
<td>Janome Sewing Machine</td>
<td>Bad loans</td>
<td>¥ 152 billion</td>
<td>¥ 2,000,000$\textsuperscript{a}</td>
<td>¥ .013</td>
</tr>
<tr>
<td>Obayashi</td>
<td>Bribery</td>
<td>¥ 290 million</td>
<td>¥ 20,000,000</td>
<td>¥ .027</td>
</tr>
<tr>
<td>Takashimaya</td>
<td>Sokaiya</td>
<td>¥ 160 million</td>
<td>¥ 170,000,000</td>
<td>¥ .557</td>
</tr>
<tr>
<td>Nomura Securities</td>
<td>Sokaiya</td>
<td>¥ 828 million$\textsuperscript{c}</td>
<td>¥ 380,000,000</td>
<td>¥ 1.321</td>
</tr>
<tr>
<td>Ajinomoto</td>
<td>Sokaiya</td>
<td>¥ 120 million</td>
<td>¥ 120,000,000</td>
<td>¥ .185</td>
</tr>
<tr>
<td>Hitachi</td>
<td>Bid-rigging</td>
<td>¥ 232 million</td>
<td>¥ 100,000,000$\textsuperscript{d}</td>
<td>¥ .030</td>
</tr>
<tr>
<td>Dai-Ichi Kangyo Bank</td>
<td>Sokaiya</td>
<td>¥ 2.2 billion</td>
<td>¥ 127,000,000</td>
<td>¥ .041</td>
</tr>
<tr>
<td>Cosmo Securities</td>
<td>Tobashi Accounting</td>
<td>¥ 69.8 billion</td>
<td>¥130,000,000</td>
<td>¥.300</td>
</tr>
</tbody>
</table>

$\textsuperscript{a}$Outstanding share data from Toyo Keizai ed., SHIKIHO (1999).

$\textsuperscript{b}$Settlement of only one director, who also agreed to return 6,000 shares.

$\textsuperscript{c}$Consolidation of three suits.

$\textsuperscript{d}$One defendant only.

The settlement data suggest three conclusions. First, cases only settle when directorial conduct is quite severe – apparently bad loans, bribery, bid-rigging, payments to sokaiya, and illegal accounting measures are necessary preconditions. To break down the 51 cases roughly by

cause, the directors of every firm in the sample (8 separate suits) accused of paying sokaiya settled. In the four cases of bribery in the sample, one settled, and one was a plaintiffs’ victory. One of the two accounting cases (“tobashi” accounting fraud and loss compensation) settled. Two of the five illegal trading cases (both against Daiwa Bank directors) were plaintiff victories, but are on appeal. By contrast, only one of the fifteen cases involving bad loans settled, and in that case the loans were made to a raider with organized crime connections. In only one of the eleven cases involving alleged bad investments or acquisitions did plaintiffs win or obtain settlement. Plaintiffs neither won nor achieved settlement in the two HIV tainted-blood cases, the two labor cases, the lone real estate contract case, or the single nuclear power case.

Second, note the large discrepancy between damages claimed and settlement amounts. Although plaintiffs in the Ajinomoto and Takashimaya cases fared relatively well, on average, plaintiffs settled for less than one-half of one percent of damages claimed.

Finally, note the settlement amount per share. In theory, the amounts listed above, when paid by the directors to the relevant firms, should increase the price per share by the relevant amounts (minus attorneys’ fees paid by the corporation). Despite the relatively high price of Japanese stocks, per share recovery in Japan appears to be even lower than it is in the United States – about one-third of a cent in Japan, compared to eighteen cents in the U.S.

To test whether plaintiffs actually receive such gains, I conducted an event study on the eight firms listed in Table 4. The returns for both days were positive, with a two-day increase of .872%, but statistically insignificant (t = 1.54). An increase of .872% represents an average gain

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34 See James Sterngold, In Japan, a Plundered Company, N.Y. TIMES, Nov. 9, 1993, at D1.
35 See Romano, supra note 2, at 62.
of approximately eight yen per share, but we cannot state with any reasonable degree of certainty that this return did not result from chance.

The above evidence suggests that plaintiffs have little economic reason to file suit. I found no statistically significant abnormal returns upon filing suit or settlement. In fact, the only statistically significant returns found were those observed when plaintiffs were required to post bond, tentatively suggesting that shareholders find some suits frivolous and wasteful of corporate assets.

The event study tests are by no means conclusive. The sample is relatively small and may not be representative of the entire market. The event dates that I examine may not necessarily be the proper period to examine, as investors may have anticipated filings, court opinions, and settlements long before the event window dates. As always, there is much noise in the market, longer event windows introduce even more noise, and it is difficult to assess causation. And the question of what exactly event studies measure is open to debate.\textsuperscript{36} Still, using standard statistical methods, my results are relatively similar to those found by both Romano and Fischel and Bradley: derivative suits, whether in the U.S. or Japan, produce few gains, or at least few immediate and direct gains, to shareholders.

III. SO WHY SUE?

Shareholder litigation in Japan, like shareholder litigation in the United States, does not appear to be motivated by direct benefits to shareholders. But if not, why sue? Even if shareholder litigation results in intangible deterrence benefits, there should be little reason for

individual shareholders to sue. In this Part, I attempt to unravel the reasons behind Japanese shareholder litigation.

This Part is the result of an examination of 140 derivative suits filed between 1993 and 1999. Of these 140 cases, 73 are listed in the Shiryōban Shōji Hōmu list used in Part II. The remaining 67 cases were not used in the Part II study because of insufficient stock price data; none of the firms are listed on the Tokyo Stock Exchange. Of these 67 cases, 23 are not listed in the database but had published court opinions or other official documents. From attorneys, court offices, and other sources, I obtained briefs and other court records on 29 cases. Through interviews, I gathered information related to fifteen additional cases.

A. Bar Benefits

One potential source of derivative litigation – and the leading cause of such suits in the United States – is plaintiffs’ attorneys. If attorneys can win sufficient fee awards, suits will have a net positive value and will proceed regardless of whether plaintiffs directly receive large benefits. So long as an attorney can find a nominal shareholder willing to lend her name to the complaint, suits will be filed.

In Japan, determining exactly what benefits accrue to attorneys in derivative actions is difficult. Most attorneys’ fee agreements are separate from settlement agreements and confidential, and there is no Japanese scholarship on point. In this section, I first describe the basics of the Japanese legal profession and attorney compensation. I then turn to the specifics of attorneys’ fees in derivative litigation, first in theory, and then in practice.

1. The Market for Attorneys. Much has been written about the structure of the Japanese legal profession. In short, lawyers are few, most are in Tokyo, and they have a monopoly over
most legal services. With half the population of the United States, Japan has approximately 17,000 licensed attorneys in comparison to their roughly 800,000 American counterparts. This simple numerical comparison is misleading for a variety of reasons, but the small number of attorneys in Japan matters in the derivative suit context because only attorneys (and pro se plaintiffs) may bring such suits.

In cartel-like fashion, the Japanese Federation of Bar Associations publishes an attorneys’ fee schedule (the “Fee Rules”) that is adopted by local bar associations. Attorneys’ fees are generally paid by each litigant and have two components: a nonrefundable retainer (chakushukin), based on the amount of damages claimed, and a “success fee” (hoshi,kin) based on the amount of damages actually received. Although not mandatory, many attorneys follow the cartel schedule to the letter, and most fees are reasonably close to the chart. Table 5 shows the basic range of these fees established in the Fee Rules:

<table>
<thead>
<tr>
<th>Plaintiff’s Damages</th>
<th>Retainer</th>
<th>Success Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to ¥ 3 million (about $30,000)</td>
<td>8%</td>
<td>16%</td>
</tr>
<tr>
<td>From ¥ 3 million to ¥ 30 million (about $30,000 to $300,000)</td>
<td>5% + ¥ 90,000</td>
<td>10% + ¥ 180,000</td>
</tr>
<tr>
<td>From ¥ 30 million to ¥ 300 million (about $300,000 to $3 million)</td>
<td>3% + ¥ 690,000</td>
<td>6% + ¥ 1,380,000</td>
</tr>
<tr>
<td>Over ¥ 300 million</td>
<td>2% + ¥3,690,000</td>
<td>4% + ¥ 7,380,000</td>
</tr>
<tr>
<td>Indeterminate economic gain = damages fixed at ¥8 million</td>
<td>¥490,000</td>
<td>¥980,000</td>
</tr>
</tbody>
</table>

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37 For example, on a per capita basis, Japan annually graduates about twice as many law-trained students as the United States. Most of these legal graduates are either employed in governmental ministries and corporations where they perform legal tasks, or serve as specialized quasi-lawyers in such capacities as tax agent, notary or scrivener.


39 Although empirical data are lacking such as those in this study are lacking for general litigation, many attorneys are said to charge a retainer of about ten percent and a success fee of about fifteen percent, except in cases with very high damages. See SONGAI BAISH GAKU SANTEI KIJUN [STANDARDS FOR COMPUTATION OF DAMAGES] 14 (Tokyo San Bengoshikai Ketsu Jiku Shori linkai ed. 1993); Zensuke Ishimura & Yuriko Kaminaga, Attorneys and Cases Involving Automobile Accidents, 9 LAW IN JAPAN 83, 106-08 (1976). Ramseyer cites sources that suggest that attorneys alternatively charge either more than or less than the Fee Rules. J. Mark Ramseyer, Lawyers, Foreign Lawyers, and Lawyer-Substitutes: The Market for Regulation in Japan, 27 HARV. INT’L L.J. 499, 524 & n. 103.
Consider how the Fee Rules would apply if the eight settled cases in the Part II Tokyo Stock Exchange dataset (see Table 4 above) went to court. In those cases, the average amount claimed was about ¥ 28 billion ($280 million), and the average damages award was ¥ 131 million (about $1.3 million). Pursuant to the Fee Rules, assuming that the base amounts are not considered “indeterminate” to the filing shareholder, the average retainer would have been ¥ 564 million (about $5.6 million), and the success fee approximately ¥ 12.6 million (about $126,000), for a total average fee of about $5.7 million. This figure suggests that if an attorney follows the Fee Rules, and if the court awards fees accordingly, compensation is lower than in the United States, but is not trivial.

But also consider how the Fee Rules would apply in all cases, not just the settled ones. According to my calculations, the average amount of damages claimed in the 51 cases in the dataset is ¥39.32 billion, or about $400 million. If Japanese attorneys applied the Fee Rules to this amount, their average retainer – the fee that they would receive simply for filing the case, regardless of their success or even their subsequent laziness – would be over $7 million. That fee would be substantially higher than the average fee initially received by attorneys in the United States, who generally are only compensated on a contingent basis.

Of course, whether attorneys will take derivative suits depends in part on the opportunity costs of turning down other work. The cartel’s Fee Rules dictate that attorneys will be compensated primarily based on damages claimed and awarded, not the difficulty or time-consuming nature of the suit. Attorneys should be more likely to accept non-derivative suits

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40 See Janet C. Alexander, Do the Merits Matter? A Study of Settlements in Securities Class Actions, 43 STAN. L. REV. 497, 541 (1991); Romano, supra note 2, at 63 (twenty to thirty percent). Both systems contain distortions by which shareholder and attorney gains create either too much or too little incentive to sue. See Reinier Kraakman et al., When Are Shareholder Suits in Shareholder Interests?, 82 GEORGETOWN L. REV. 1733 (1994).
with equal damage payouts and greater chances of success that produce the same income with less risk and less work.\footnote{See John C. Coffee, Jr., \textit{Understanding the Plaintiff’s Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions}, 86 \textit{COLUM. L. REV.} 669, 704-12 (1986).}

2. \textit{Court-Awarded Derivative Suit Fees}. Pursuant to the Commercial Code, attorneys are entitled to a “reasonable amount” of attorneys’ fees upon plaintiff’s motion. But because of the lack of cases litigated to final judgment even after the 1993 Commercial Code revisions, it is difficult to determine precisely what constitutes a “reasonable amount.” The issue raised concerns as the rules were undergoing revision in 1993. According to Japan’s leading corporate defense lawyer Hideaki Kubori:

When the amount of economic gain is indeterminate, the Fee Rules provide for [a base amount of ¥ 8 million; ¥ 5 million pre-1995]. Of course, the amount can be raised or lowered based on the difficulty of the case, but looking generally at the problems of argument and proof involved in derivative suits, I don’t think that this level gives much economic incentive to attorneys to bring cases. I think that courts should consider the fact that it’s the corporation that stands to gain large amounts from these suits, and base awards of retainers and success fees pursuant to Section 268-2 on the corporation’s gain.\footnote{Shinsaku Iwahara et al., \textit{Zadankai, Kabunushi Daihyû Soshû Seido to Zaizen to Kongo no Mondai ten [Roundtable, Improvement of the Shareholder Derivative Suit Mechanism and Future Problems]}, 1329 \textit{SHÅI HÅMU} 4, 17 (1993)(statement of Hideaki Kubori).}

While the statement is somewhat curious coming from a \textit{defense} attorney, it reflected the views of many other commentators, who agreed that fixing the base amount as an indeterminate amount would not result in sufficient incentives for attorneys.\footnote{See, e.g., Fumio Koma, \textit{Kabunushi Daihyû Soshû Mondaito Taio [Application and Problems of Shareholder Derivative Suits] 68-69} (1994); Akio Takeuchi, \textit{Kabunushi Daihyû Soshû no Katsuyô to Ran’yô BÅshi [Shareholder Derivative Suit Activity and Abuse Prevention]}, 1329 \textit{SHÅI HÅMU} 34, 37-8 (1993).} Other commentators noted that the Fee Rules, however applied, would function to prevent attorneys from demanding high damages from corporations, as increased damage claims would lessen a plaintiff’s ability to pay the corresponding retainer. Few commentators...
offered decisive and feasible alternative solutions, and in their absence, parties routinely cited the Fee Rules as the potential basis for award in their briefs, and courts used the Fee Rules when deciding bond motions to demonstrate the burden placed on defendant directors.

In 1998, the Kobe District Court decided the only case directly on point, *Këno v. Këno Chemical Co.* (pseudonyms). In that case, the shareholder-plaintiffs argued that the amount of damages should be based on the Kobe Bar Association’s version of the Fee Rules. Because the damages initially claimed were ¥118.4 million ($1.18 million), and the damages eventually awarded were ¥147,376,766 (about $1.5 million), the appropriate “reasonable amount” of fees, plaintiffs argued, is ¥11,663,302 (about $116,000). The court agreed with the plaintiffs, finding that the appropriate base amount for calculating fees was the amount of damages requested by the plaintiff. In doing so, the court expressly rejected the claim that because the plaintiffs’ “economic gain” is indeterminate, the fee should be calculated based on an indeterminate amount of damages, which would have resulted in the lower fee of ¥147,000 ($14,700, see Table 5). The court then held that an amount approximately equal to that stated in the Fee Rules was

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44 One possible solution was to mimic the approach taken in citizens’ suits, suits brought by citizens on behalf of a municipality against public officials. Scholars and judges had long recognized parallels between citizens’ suits and derivative suits on the issue of litigation fees, which follow the “indeterminate damages” rule and consequently required only ¥ 8200 in fees. See Chih Æ Jichi Hë [Local Autonomy Law], Law no. 67 of 1947, Art. 242-2(7); see also Nishio v. Kuwabara, Supreme Court, 370 HANREI TIMES 46 (Judgment of Mar. 30, 1978)(noting similarities) Akio Takeuchi, Torishimaiyaku no Sekinin to Daihyë Soshë [Directors’ Liability and Derivative Suits], 99 GÉKKAN HÈGAKU KYÈSHITSU 6, 14-6 (1988)(arguing for ¥ 8200 based on similarity); A similar approach could have been taken with attorneys’ fees. At least one Japanese court has held (in 1994) that in determining fees, plaintiffs may rely on the Fee Rules, the amount may be predicated on the amount of damages paid as opposed to an indeterminate amount of damages received, and that a thirty-percent increase based on case difficulty is appropriate. Matsuura v. Osaka, Osaka District Court, 893 HANREI TIMES 142 (Judgment of June 28, 1994).


46 See, e.g., Suzuki v. Itoh, Nagoya High Court, 1531 HANREI JIHO 134 (Judgment of Mar. 8, 1995); Nupis Hong Kong Ltd. v. Iizuka, Urawa District Court, 1504 HANREI JIHO 121 (Judgment of Aug. 29, 1995).

“reasonable,” and awarded a fee of ¥ 11,600,000 (about $116,000). This lone opinion thus suggests that attorneys that are successful in derivative actions can expect to receive something close to what the Fee Rules dictate.

3. Settlement Practice. The Kobe District Court’s judgment may not be dispositive. No appellate court has ruled on the matter, and although the Japanese judiciary is relatively homogenous, an opinion by the Kobe Court is not controlling in the Tokyo or Osaka district courts, where the bulk of derivative litigation occurs. Accordingly, I look to settlement practice for answers.

Settlement practice suggests that attorneys in successful derivative suits are compensated beyond the $14,700 prescribed by the Fee Rules for “indeterminate damages” cases, but perhaps less than the full Fee Rules amounts authorized in the Kobe District Court’s decision. The first in-court derivative action settlement was the Nihon Sunrise case. Plaintiff-shareholders sued three Nihon Sunrise directors, alleging that breaches of the duty of care occurred when the directors authorized the company to borrow an amount of money that was disproportionate to its ability to repay. After the plaintiffs prevailed in district court, winning ¥ 295 million, the parties settled in Tokyo High Court for ¥ 130 million ($1.3 million).

The settlement agreement provided for attorneys’ fees. Plaintiffs’ attorneys stated that given the split of opinion regarding fees at the time of the settlement (1994), they were only able

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48 Japanese law does not require judicial approval of settlements or notice to shareholders of settlement. See generally Tatsuo Ikeda & Masahiro Nakagawa, Kabunushi Daihyo Soshin Okeru Wakai [Settlement of Derivative Actions], 1062 JURISUTO 66 (1995).

49 Yoshitake v. Todani (Nihon Sunrise Case), Tokyo District Court, 1354 SHIJI HOMU 134 (Judgment of Mar. 31, 1994); Yoshitake v. Todani (Nihon Sunrise Case), Tokyo High Court, 1480 HANREI JHO 154 (Judgment of Sept. 21, 1993).
to negotiate a reduced total fee of nine percent, or roughly ¥ 11.7 million ($117,000). Under
the Fee Rules, the retainer alone would have been nearly ¥ 10 million. Considering that this fee
was to be shared among four elite attorneys for several months of work, it is a low amount in
comparison both to U.S. fees and to fees that could be earned by those attorneys in Japan in non-
derivative actions. Or to put it more bluntly, as the lead attorney in that case told me, “we really
didn’t make much on that thing at all.”

Unfortunately, public settlement agreements such as this one are rare. I examined twelve
reported settlement agreements and found no mention of attorneys’ fees other than an occasional
general provision as to which party was to bear “litigation costs.” For whatever reason, attorneys
apparently prefer to have attorneys’ fee arrangements documented in separate agreements that
are not readily available.

4. What do Attorneys Actually Charge? Anecdotal evidence suggests that in practice,
many derivative suit attorneys reduce their retainers. In the Janome Sewing Machine case, for
instance, in which damages claimed were ¥ 152 billion ($1.5 billion), attorneys reportedly
accepted a retainer of only ¥ 3 million ($30,000). The retainer under the Fee Rules would have
been over ¥ 3 billion ($30 million). But attorney practice varies widely, and differences in
practice and motivation may be observed between elite and non-elite lawyers.

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50 Naoya End et al., *Nihon Sanraizu Kabunushi Daihyō Soshū Jiken no Ichiban Hanketsu to Wakai* [Nihon
51 Interview with Naoya End, November 11, 1999.
52 Suzuki v. Yasuda (Janome Sewing Machine Case), Tokyo District Court, 125 SHIRY&BAN SHIIH&MU 184
(Judgment of July 8, 1994).
53 Mitsue Aizawa et al., *Zadankai, Kabunushi Daihyō Soshū no Tetsuzukihōteki Kenze* [Roundtable on
Examination of Shareholder Derivative Suit Procedural Law], 1062 JURISUTO 8, 15 (1995)(statement of Mitsue
Aizawa).
a. *Elite attorneys.* At least one group of attorneys consistently accepts derivative actions on a reduced-retainer basis. Founded in February 1996 and based in Osaka, the Shareholder Ombudsman (*Kabunushi Onbuzuman*) organization consists of about twenty elite lawyers, as well as accountants, academics, and investors. Shareholder Ombudsman has accepted several of the more high profile cases in Japan, including derivative actions against directors of Takashimaya Department Store, Sumitomo Corporation, Dai-Ichi Kangyo Bank, Nomura Securities, Yamaichi Securities, Ajinomoto, Japan Airlines, and Kobe Steel.

Shareholder Ombudsman member attorneys informed me that the group does not calculate its fee in accordance with the Fee Rules, choosing instead to charge a retainer of only ¥300,000 to ¥500,000 ($3,000 - $5,000). Although this is still a significant amount for many plaintiffs, the organization has ongoing relationships with several shareholders who regularly lend their names to cases. If the plaintiffs win, the corporation pays the attorneys’ fee based on the Fee Rules. A portion of the fees goes to the attorneys involved with the case, but most money flows back to the organization. Although I was unable to gather data on all Shareholder Ombudsman cases, I obtained attorneys’ fee amounts for three of the Table 4 settlements and listed them in Table 6.

<table>
<thead>
<tr>
<th>Case</th>
<th>Settlement Award</th>
<th>Fee Under Fee Rulesa</th>
<th>Fee Actually Paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Takashimaya</td>
<td>¥170 million ($1.7 million)</td>
<td>¥16.47 million ($164,700)</td>
<td>¥19.95 million ($195,000)</td>
</tr>
<tr>
<td>Ajinomoto</td>
<td>¥120 million ($1.2 million)</td>
<td>¥12.87 million ($128,700)</td>
<td>¥12.87 million ($128,700)</td>
</tr>
<tr>
<td>Obayashi</td>
<td>¥20 million ($200,000)</td>
<td>¥28.17 million ($281,700)</td>
<td>¥2.5 million ($25,000)</td>
</tr>
<tr>
<td>Average</td>
<td>¥103 million ($1.03 million)</td>
<td>¥19.17 million ($191,700)</td>
<td>¥11.77 million ($117,000)</td>
</tr>
</tbody>
</table>

*aCalculated using damages claimed as stated in Table 4.*

These fees, which average about eleven percent of the settlement award, are lower on average than those dictated by the Fee Rules. But note that the relation of fees paid to fees under the Fee Rules is not uniform. While the Ajinomoto settlement was exactly as dictated by the Fee Rules, Obayashi was lower, and Takashimaya was higher (based largely on the fact that the
defendants agreed to a higher settlement award than damages initially claimed to include newly incurred damages).

The data in Table 6 also suggest two rent-seeking strategies of the Shareholder Ombudsman group. First, note that these cases are winners. In order to receive more than a trifling portion of a reduced retainer, organization attorneys must win the case or obtain a settlement. But Shareholder Ombudsman attorneys have great shot selection. By selecting their cases carefully – choosing, for instance, a number of sokaiya cases, while somehow avoiding many poor investment cases in which the business judgment rule is most likely to apply – the organization increases the chance that it will receive large fees. Other than general claims about case selection by participating attorneys, I have no precise data on cases actually turned down by the organization. But the fact that after extensive publicity campaigns, the organization accepts a high percentage of cases that would seem to generate maximum profit is suggestive, at least, of an overall success-maximizing strategy.

Second, the organizational structure chosen by the organization leads to profit maximization. Because of the Fee Rules, attorneys operating as individuals might be at least as well off accepting other less complicated cases (with greater chances of success). Pooling resources among several attorneys to handle potentially more time-consuming and risky cases helps those attorneys diversify their risk portfolios. Without Shareholder Ombudsman to help attorneys diversify their case portfolios, it is possible that some derivative suits would never be filed.

Still, in my discussions with attorneys from Shareholder Ombudsman, they, and other attorneys not affiliated with the organization as well, stated that they take on cases on a reduced-fee basis out of a sense of justice. Organization literature states that the group only takes on
causes and cases that have “social value.” In addition to cases involving financial misdeeds, Shareholder Ombudsman has also been active in pursuing cases for the rights of disabled persons, and has also explicitly sought apology from wrongdoers in addition to monetary damages on behalf of shareholders.\(^5^4\)

I do not deny that some attorneys are genuinely and rationally altruistic. In fact, given the relative wealth of elite attorneys in Japan, it is likely that some are truly motivated by altruism. Still, an examination of attorney incentives illuminates several non-altruistic motives to accept cases on a reduced-fee basis. Attorneys are likely to be rewarded by what Landes and Posner call “the recognition factor.”\(^5^5\) Because of a ban on attorney advertising in Japan,\(^5^6\) the recognition and prestige that accompany representation against powerful corporate interests could potentially generate future gains. Organization-affiliated attorneys stated privately to me that while justice matters, the recognition factor matters as well.

Reputation may be particularly important for derivative litigation given the niche market factor. Many elite attorneys, or at least those at elite law firms, primarily represent corporate interests. Attorneys who can develop a reputation for bringing suits against corporations, even on a pro bono basis, may be likely to attract future left-leaning or anti-corporate clients (such as labor unions). Although such attorneys may be sacrificing future opportunities to work for corporate clients, many attorneys with whom I spoke, including those who made strong altruistic claims, stated that the niche market factor is important. In this connection, it is interesting to

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\(^{5^4}\) See Songai Yue no Kaiko ha Yursareruka? [Shall We Allow Dismissal Based on Handicap?], in KAISHA NO SHAKAI SEKININ [CORPORATE SOCIAL RESPONSIBILITY] 24 (Kabunushi Ombudsman ed. 1998); Ajinomoto Settlement Agreement, in KAISHA O HAKARU [MEASURING CORPORATIONS] 63 (Kabunushi Ombudsman ed. 1999).


note that most derivative suit attorneys are from smaller firms – none are from the relatively large Tokyo powerhouses, who traditionally represent corporate clients.

While junior attorneys also experience reputation effects from publicity, as one such attorney explained to me, because of their youth, they “must be paid some amount, or they simply can’t afford to do it.” Junior attorneys also receive additional perks in exchange for their fee. Unlike most junior attorneys in Japan, derivative suit attorneys receive the ability to work on interesting cases and to tell their friends and future clients that they are suing some of Japan’s largest and most prestigious corporations.

b. Non-elite Attorneys. At the other end of the spectrum from Shareholder Ombudsman are a small handful – if that many – of attorneys who often are straightforward in their acceptance derivative cases for reasons that more typically drive shareholder litigation in the United States – attorneys’ fees. These attorneys are not elite lawyers like the Shareholder Ombudsman group, an expected result given the fee rule incentives for elite attorneys to take the best and easiest cases. After elite attorneys have taken the best, these non-elite attorneys are often stuck with the low-return, high-risk losers. I determined that only 11 of the 140 cases – besides those litigated by Shareholder Ombudsman elites -- involved attorneys who appeared to use the case either for publicity or explicitly for non-discounted attorneys’ fees, but that determination is highly subjective and relies mostly on information on reputation gleaned from interviews.

One Japanese attorney, Hideto Iida, has been involved in several large derivative cases, including suits against directors of Green Cross, Nomura Securities, and Sumitomo Corporation, but until recently, he had never won a case. It is possible to ascribe a non-monetary motivation to each of Iida’s cases, especially given his low success rate. Consider Iida’s statement to the
Wall Street Journal that in order to find a plaintiff to sue Sumitomo, he “began dialing through his secret list of 10 big investors.” Iida might have begun dialing because he is rent-seeking, or because he has a passion for justice.

Most observers emphasize the former over the latter. Rightly or wrongly, Iida is widely regarded in the media, Japanese corporate executives, and in fact by other attorneys who bring derivative suits as motivated by some combination of attorneys’ fees and advertising. Iida and Shareholder Ombudsman once attempted a collaborative relationship. It failed, according to an organization attorney, because Iida and Shareholder Ombudsman had “different objectives and motivations.”

Iida and I had some general conversations, but despite repeated attempts, he did not discuss the specifics of his fee arrangements with me. He told the Wall Street Journal in 1996 that he earned only $300 total in fees from shareholder litigation, and the Journal described his office as “closet-sized.” But in September 2000, Iida’s economic situation showed potential for change. The plaintiffs in the $775 million Daiwa Bank case, as it turns out, are represented by Iida and three other attorneys. If plaintiffs win on appeal or the case ultimately settles, Iida may gain handsomely.

Few attorneys are willing to take the chances that Iida has, and those that do usually remain in closet-sized offices. But for the attorneys who can identify winners, there apparently is profit to be found here. If potential profits to attorneys outweigh costs, we might expect attorneys to enter into Coasian transactions in which they award a portion of their fee to the plaintiffs to induce them to sue. I have seen confidential and (and presumably privileged) internal documentation of one case in which the attorneys gave the plaintiff approximately

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$2,000 from the attorneys’ fee received from the corporation. Two plaintiffs that I interviewed regarding separate suits also spoke of such arrangements.

The available evidence strongly suggests that the kickback practice is not rooted in the Japanese gift-giving tradition. Independent attorneys with whom I discuss the issue are amazed to hear that such a practice exists; most thought it to be clearly illegal, and all thought it inappropriate. Although the Commercial Code, the Attorneys’ Law and the Attorneys’ Code of Ethics contain no specific prohibition of such a practice, and no disciplinary proceeding record on point exists, the fee-kickback practice does indeed rest on shaky legal ground. When I asked the Federation of Bar Associations for a hypothetical declaratory judgment on the issue, I was told that it violates an attorney’s duty to his client, rules that prohibit attorneys from having a stake in the judgment, and the Commercial Code – regardless of whether the arrangement is pursuant to a prior agreement.58 A tradition that is secret, illegal, and against attorney norms would be strange indeed, and I suspect that it continues because of rent-seeking, not benevolence. “If I wanted to say thanks,” one attorney succinctly declared, “I’d send them a melon or a bottle of wine.”

These clandestine practices – unwritten attorneys’ fee agreements and kickbacks to plaintiffs – arouse my suspicions that perhaps there are more incentives for attorneys and plaintiffs than meets the eye. Secret benefits would be especially easy to achieve given the lack of a judicial approval and publication requirement for settlements. Although very few cases

58 Telephone interview of June 2, 2000. Although the Federation of Bar Associations did not cite a specific provision, the duty issues presumably arise from articles 56 of the Attorneys’ Law and articles 4, 8, and 14 of the Code of Ethics. The Federation cited article 28 of the Lawyers’ Law and article 16 of the Code of Ethics for the rules against an attorney having a stake in the judgment. The violation of the Commercial Code is said to arise from the fact that the Code contemplates the entire award being awarded to the attorney. Id. Although I normally conduct all my own interviews, and find that I often get more information than a Japanese interviewer would, in this case I thought it better to enlist the aid of a Japanese attorney. Special thanks to Noboyuki Sakuraba for assisting with this matter.
have actually settled or been withdrawn by plaintiffs in the absence of an adverse ruling on a bond motion, it would not be surprising in some suits to find hidden economic benefits such as direct payments from directors to plaintiffs or various lawyer-client contingency arrangements. But at least in the cases of large, public corporations in which data is easily available and whose events the media follow, I have no direct evidence (other than attorneys’ fee kickbacks) of questionable payments.

B. Residual Explanations

Attorney motivations appear to have the greatest explanatory power in analyzing why Japanese shareholders sue. At least four other reasons play supporting roles: non-monetary motives, sokaiya suits, insurance-settlement motivations, and suits against non-public (close) corporations.59

1. Non-Monetary Motives. Some suits appear to reflect little or no obvious individual economic motivation for any party. These suits are motivated by social movements, spite, moral disdain, altruism, fairness, justice, and desire for public vindication.

Perhaps the suits with the clearest non-monetary concerns are those brought by environmental activists. In the Chubu Electric case,60 for instance, shareholders demanded that

59 A fifth reason occasionally mentioned is the use of derivative suits as a weapon by foreign investors in hostile takeover battles for Japanese companies. See http://www.tabisland.ne.jp/epson/scrum/j_kabu.htm (last checked Sept. 23, 1999, site taken down, printout on file with author); http://www.geocities.co.jp/WallStreet/6870/990708.html. Although foreign takeover attempts have occasionally led to derivative suits, see Nupis Hong Kong Ltd. v. Iizuka, Urawa District Court, 1504 HANREI JIBO 121 (Judgment of Aug. 29, 1995), the threat appears to be exaggerated, as I found no cases in which derivative suits were used as a weapon by foreign investors (and no examples of suits brought by non-Asian persons or entities). The speculation that suits would be used for such a purpose may be grounded in a popular business novel by attorney Shin Ushijima about an U.S. corporation’s attempt to use such tactics. See SHIN USHIJIMA, KABUNUSHI DAHYÔ* SÔSHÎ 87 (1998)(reprint edition 2000)(“Just as Japan bought Rockefeller Center and Hollywood, we’re going to buy Akagiya. We won’t spend a cent. It’s magic.”)

60 Nakagawa v. Matsunaga (Chubu Electric Power Co. Case), Nagoya High Court, 169 SHIRYÔBAN SHÔJI HÔMU 240 (Judgment of Nov. 17, 1999).
management pay back to the company ¥ 200 million ($ 2 million) that was given to a local fishery association to as compensation for future fishing losses to result from a feasibility study for a nuclear power plant. The anti-nuclear plaintiffs argued that the payment was a bribe, and that there was little prospect of the feasibility study being completed. (The court disagreed.) The goal, of course, was not payment per se, but prevention of plant construction.

Activist cases aside, my interviews suggest three general non-monetary factors at work. First, some plaintiffs expressed anger over corporate scandals. Second, some saw suits as a method of expressing their moral opprobrium and sense of justice. As one plaintiff explained to me, “I don’t expect to make any money off of this. I just want those guys to know that what they did was wrong and that they can’t do that sort of thing.” Third, some took pride in their role as corporate cops, and seemed to enjoy contributing to the welfare of others.

It is difficult to assess exactly how many of the cases are linked to such motivations, or to what extent suits with ties to organized citizens’ movements are motivated by non-monetary incentives. Some plaintiffs clearly appear to be suing for non-monetary reasons (given the data in Part II, many must), and anger can probably explain a residuum of suits in any system.

I interviewed ten individual plaintiffs suing directors of large public corporations. Although the sample is by no means scientific, it is useful in sorting out plaintiff and attorney motivations. All ten stated that they were suing for some sort of non-monetary reason, usually to “teach those guys a lesson.” Each plaintiff expected to incur no monetary costs; he expected to win or obtain a large settlement (eight of the cases involved criminal action by the director or a related party), and accordingly expected the company to pay their attorneys’ fees and the directors to reimburse even their ¥ 8200 in filing fees.
Of the ten plaintiffs, two stated that they expected to receive compensation in the form of a distribution from their attorneys – clear monetary incentives. One plaintiff was a large blockholder (suing his brother, no less) who expected to gain from an increase in the value of his shares – again, clear monetary incentives. The remaining seven plaintiffs have no clear monetary incentives. Only one plaintiff of the seven, a retired bank president who was the least forthcoming of my interviewees in volunteering answers, paid a “full price” retainer to his attorney. Four plaintiffs paid reduced retainers to their attorneys, and two paid no retainer at all. Each of these six plaintiffs told me that he would not have paid full price, and one explicitly offered this underlying reasoning: “I may be angry, but I’m not stupid. The only one who will profit here is my attorney, and he is in charge. I get no profit, and I have no say. I want those guys to pay, but I’m just along for the ride.”

Other plaintiffs and attorneys made similar statements that suggest the dominant role of attorney incentives. One prominent attorney told me before my plaintiff interviews started, “Of course, they’ll all tell you that they’re suing because they want justice. Most of them actually do want justice, but who doesn’t? We all want justice. Of course I coach them to make those statements to the media and so on, but most of them believe it anyway . . . . The truth is that justice or no justice, attorneys want winning cases, and if they can’t get a winner, they’ll take what’s left.”

Without delving far more deeply into the psyche and veracity of Japanese plaintiffs and attorneys than I am prepared to go, it is difficult to assess conclusively whether these ten suits proceeded because of anger, attorney incentives, or some combination of both. In three of the ten cases, plaintiffs had monetary motives, but the blockholder case surely is a rare one. In seven of the ten cases, plaintiffs had no monetary incentive to sue. The evidence presented in Part III
strongly suggests the existence of attorney incentives, and plaintiff and attorney statements support the Part III evidence. Given the interview evidence, the more tangible nature of attorney incentives, and a necessarily subjective judgment about the sincerity (or more accurately, the lack thereof) of the emotions expressed by some the plaintiffs whom I interviewed, I find a dominant role for attorney incentives to be more plausible in the majority of cases than the evidence for plaintiff non-monetary motivations.\textsuperscript{61} It is certainly possible, and I would suggest likely, that plaintiffs, like their lawyers, have multiple and complex motivations, but the evidence suggests a more dominant role in most cases for monetary incentives.

2. Sokaiya. A \textit{sokaiya} (literally, “general meeting operator”) is usually a nominal shareholder who either attempts to extort money from a company’s managers by threatening to disrupt its annual shareholders’ meeting with embarrassing or hostile questions, or who works for a company’s management to suppress dissent at the meeting. As I have discussed elsewhere, sokaiya have historically flourished in Japan because noncompetitive Japanese corporate law and governance institutions lead to low levels of corporate disclosure.\textsuperscript{62} With the lowering of filing fees in 1993, a few sokaiya branched out to derivative suits as a form of business.

Perhaps the most famous of these “derivative-suit sokaiya” is the former sokaiya labeled in court opinions with the pseudonym “Akira Suzuki.”\textsuperscript{63} One of Suzuki’s earlier suits was

\textsuperscript{61} Empirical evidence from the United States further suggests that at least in the context of trials, non-monetary interests tend to arise in limited and specific circumstances, such as when real wounds to self-esteem and damages to reputation are suffered. \textit{See} Samuel R. Gross \& Kent D. Syverud, \textit{Don’t Try: Civil Jury Verdicts in a System Geared to Settlement}, 44 UCLA L. Rev. 1, 57-9 (1996).


\textsuperscript{63} The name “Akira Suzuki” is somewhat similar to “John Doe” in the United States. Thus not all cases that list Akira Suzuki as a plaintiff are filed by the sokaiya that goes by that name. Further complicating matters, the plaintiff in the Janome Sewing Machine case, \textit{see supra} note 52, has the given name Akira Suzuki, phonetically identical but written with different Japanese characters.
against Tokai Bank directors.\textsuperscript{64} As the defendant directors explained in their bond request motion, “Due care must be given to the fact that the lowering of filing fees leads to shareholders who bring derivative suits for personal gain, derivative suits by those who hold grudges, and demonstration derivative suits by ‘occupational special shareholders’ (so-called sokaiya).”\textsuperscript{65}

Suzuki, they argued, fit the classic profile of a sokaiya:

> Beginning at least by 1984, the plaintiff began to work as an “occupational special shareholder,” attending the shareholders’ meetings of listed companies, making unruly outbursts, making motions and amendments, and wasting time with repeated questions. . . . At the 1988 Sumitomo Bank shareholders’ meeting, he proposed reducing management compensation to zero, at the 1990 meeting, he made inappropriate remarks like “the moderator is a puppet,” and at the 1991 meeting he yelled, “you’re not qualified to be a moderator.” At every meeting, in the name of “questioning,” he ignores other shareholders to raise his own opinions, does not listen to the moderator, behaves with impudence, and throws the meeting into confusion solely to demonstrate as an “occupational special shareholder.”\textsuperscript{66}

In a derivative suit brought by Suzuki against the directors of Tokyo-Mitsubishi Bank, the court noted in its granting of plaintiffs’ bond motion that Suzuki “has filed seven corporate suits, and in each of them he has either lost, withdrawn the suit, or lost the case when he refused to post bond; he does not have a single sincere lawsuit.”\textsuperscript{67}

> It is unclear exactly how many sokaiya-related suits have been brought.\textsuperscript{68} It appears to be a relatively small number; even the seven suits cited by the court as being brought by Suzuki do

\textsuperscript{64} Suzuki v. It\nobreakleft( Tokai Bank case\nobreakright), Nagoya District Court, 119 SHIRY\nobreakleft( BAN SH\nobreakleft( JI H\nobreakleft( MU 188 (Jan. 26, 1994).

\textsuperscript{65} Motion of Defendants, Oct. 18, 1993, Suzuki v. It\nobreakleft( Tokai Bank Case\nobreakright), Nagoya District Court, in 175 BESSATSU SH\nobreakleft( JI H\nobreakleft( MU 450, 452 (1995).

\textsuperscript{66} Id at 45-51.

\textsuperscript{67} Suzuki v. Ifu (Tokyo-Mitsubishi Bank Case), Tokyo District Court, 196 BESSATSU SH\nobreakleft( JI H\nobreakleft( MU 322, 324 (Judgment of June 25, 1996).

\textsuperscript{68} Such suits were brought even before the 1993 revision. \textit{See} K\nobreakleft( no v. Yoneda (Nagasaki Bank Case), Nagasaki District Court, 1393 HANREI JIH\nobreakleft( 138 (Judgment of Feb. 19, 1991).
not appear to all be derivative suits. Of the 140 cases that I examined, 10 appeared to have some sokaiya link.

Sokaiya whom I interviewed stated that while there is little direct profit in derivative suits (especially because they must chance civil liability for bringing frivolous claims), the lowering of filing fees has increased the credibility of their threats to file suit and to use the court as a public forum for sharing sensitive corporate information. Because of high response costs, corporations sometimes pay to rid themselves of nuisance suits.69 Because of the danger of public release of information, some corporations apparently pay for silence. These threats and settlements never become public documents, but can help sokaiya reap significant rewards.

Finally, it is at least interesting that the number of derivative suits has risen as the number of working sokaiya has fallen. Of course, the phenomena may be unrelated. But if they are related, I find two explanations likely. First, the increase in derivative suits against directors who pay sokaiya may in fact be effective in reducing sokaiya activity. Second, legitimate plaintiffs may be making use of information that was formerly the exclusive province of sokaiya blackmail. If the former is true, derivative litigation in Japan may have some positive deterrent effect not on managers, but sokaiya. If the latter is true, the channeling of negative information from privately-ordered sokaiya blackmail to legitimate state-backed enforcement institutions may be a positive feature of the Japanese mechanism.70

3. Insurance. Japanese directors’ and officers’ (D&O) liability insurance has gone from being unheard of to being widely used. In 1994, 400 companies had policies, an increase of

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500% from 1993. By 1999, 70 to 80 percent of listed companies were said to have policies, most in aggregate amounts of 100 to 500 million yen ($1 to $5 million). Because of relatively low risk in Japan, premiums are relatively low compared to the United States. According to the Nihon Keizai Shinbun newspaper in 1993:

> For companies listed in the second section of the Tokyo Stock Exchange, for coverage of ¥ 1 billion [$ 10 million], the premiums are generally only in the millions of yen ($ tens of thousands). If you consider this as a per-executive cost, the cost is about the same as the annual insurance premiums on a luxury car. For large firms in the first section, for coverage of ¥ 1 billion, even including their subsidiaries, the premium is only in the ten millions.

Even in 1999, the per-executive annual cost of insurance is said to be ¥200,000 to ¥300,000 ($2,000 to $3,000). Still, because of the increase in the numbers of policies written, D&O insurance is increasingly profitable, with gross premiums rising from ¥ 1.7 billion ($17 million) in 1993 to ¥ 4.8 billion ($48 million) in 1997.

Because of the increased prevalence of insurance, it could be that directors face a moral hazard problem, and consequently commit more punishable acts. But note that while the number of polices written has skyrocketed, the amounts of coverage, at least pre-Daiwa, have remained

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72 HIDEAKI KUBORI ET AL., *TORISHIMARIYAKU NO SEKININ [DIRECTOR LIABILITY]* 71 (1999); *Kyogaku Baishō* Bsei e Kigyō Hashiru [Companies Run to Defenses Following Huge Damage Award], Nihon Keizai Shinbun, Oct. 23, 2000, at 5.

73 KABUNUSHI NO HANRAN 56 (Nihon Keizai Shinbun ed. 1993); see also KABUNUSHI DAIHYŌ SOSHŌ TO KAISHA YAKUIN BAISHI SEKININ HOKEN NO KAISETSU [COMMENTARY ON SHAREHOLDER DERIVATIVE SUITS AND D&O INSURANCE] 21 (Mitsui Kaijitai Kasai Hoken Kabushiki Kaisha ed. 1994)(Mitsui Marine & Fire Insurance publication listing annual premiums of ¥500,000 for an entire board of 20 directors, or ¥25,000 ($250) per director). Note that these amounts are far lower than the damages awarded in the Daiwa case (¥83 billion). Coverage limits in 2000 were said to be in the range of 2 to 3 billion yen. See Daiwagin Kabunushi Daihyō Soshō, Chīsai Hanketsu, supra note 31.

74 KUBORI ET AL., supra note 19, at 71.

75 Id.
relatively trivial, suggesting that insurance has not led to more punishable acts. Most Japanese companies also attempt to mitigate moral hazard problems by requiring directors to contribute personally a percentage of the premium (not necessarily an odious requirement if compensation is raised accordingly).

The increased prevalence of insurance might also suggest that plaintiffs are more willing to bring suits against management because settlements will be more forthcoming from insurance companies than they would be from individuals. While there may be some truth to this, if it were a widespread motivation, we might expect to see many more settlements than we currently observe.

4. Close Corporations. This Article has explored why derivative litigation arises in large, public Japanese corporations. But ninety-nine percent of corporate Japan is small- and medium-sized enterprises, and a large number of derivative suits are filed against small private “close” corporations.

There are no reliable data on how many of the 286 suits pending at the end of 1999 were against such close corporations. The Shiryaban Shijihamu database on which I rely in Part I lists 73 post-1993 suits, of which 56 were Tokyo Stock Exchange companies, and includes every case filed against a major Japanese corporation. Assuming that the data are biased in favor of large companies, it seems reasonable to assume that a large portion of the unreported cases are

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76 See generally John E. Core, The Directors’ and Officers’ Insurance Premium: An Outside Assessment of the Quality of Corporate Governance, 16 J. L. ECON. & ORG. 449 (2000)(finding a significant association between D&O premiums and governance quality). Soon after Daiwa, interest arose in raising coverage amounts to 10 billion yen ($100 million). Kyogaku Baish, Bsei e Kigy Hashiru [Companies Pursue Defenses Following Huge Damage Award], NIHON KEIZAI SHINBUN, Oct. 23, 2000, at 5.


against close corporations. Of the 140 cases that I collected, 48 were against privately held corporations, but my database may be biased in its inclusion of the 73 Shiyraban Shëji Hëmu cases. One Japanese scholar has written that more than half of the suits involve privately held corporations,\textsuperscript{79} while my interviewees offered educated guesses of 30 to 40 percent.

An examination of the close corporation situation reveals an interesting comparison to that of public corporations. First, more plaintiffs might have non-monetary motivations. Most of these suits reflect corporate internal fights, either among relatives or between old and new management groups.\textsuperscript{80} Social protest aside, we would at least expect more emotional detachment from shareholders in larger public corporations with fewer interpersonal ties to management. Second, plaintiffs in small corporations often have greater incentives to sue than shareholders in large corporations, as their larger percentage holdings suggest that they stand to gain a larger increase in share value from a payment of damages to the corporation. None of the suits against large public corporations that I observed were brought by large blockholders, who presumably have other means of coercion. Third, plaintiffs in small corporations often have greater access to inside information, which, given the secrecy that clouds many Japanese corporations, may lead to increased litigation.\textsuperscript{81} Finally, although hard data are lacking, many of the close corporations whose directors are sued, and particularly the sub-category of family-held corporations, have several large shareholders that are of different relative sizes. Recent theoretical and empirical work focusing on shareholder conflict in close corporations suggests


\textsuperscript{80} See Suzuki v. Yasuda (Janome Machine Case), Tokyo District Court, 1504 HANREI JIBO 121 (Jul. 22, 1994).

\textsuperscript{81} For an example, see Peter Landers, Unbuilt Golf Course Lands Japanese Firm in Fight Over Secrecy, WALL ST. J., June 13, 2000, at 1 (suit against Mitsukoshi by former board member relating to secret 59 billion yen expenditure). Although data are limited, I find no patterns in plaintiff success rates. On Japanese corporate secrecy, see West, supra note 62.

Curiously, many cases involving directors of small corporations involve corporate plaintiffs with contractual ties to the corporation in addition to their shareholdings.\footnote{Nippon Hissors Case (no party names given), Tokyo District Court, 175 SHIRYISING BAN SHIJI HIME 277 (Judgment of Sept. 24, 1998); Fukuoka Fish Market v. Kino (Fukuoka Fish Market Case), Fukuoka District Court, 944 HANREI TIMES 247 (Judgment of Jan. 30, 1996); Kajima Ksan K.K. v. Hoshino (Neo Daikyless Driving School Case), Kobe District Court, 901 HANREI TIMES 233 (Judgment of Nov. 17, 1995); see also Naoto Nakamura, *Kabunushi Daihyosho no Saikin no Jûkysû* [Recent Developments in Shareholder Derivative Litigation], 1512 SHIJI HIME 11, 13 (1998). I found no cases of inter-keiretsu suits among large corporations.} This finding has interesting implications for relational theories of corporate governance in Japan and elsewhere. Relational theory holds that “the increase in derivative litigation is consistent with more arm’s length relationships among Japanese managers and at least some of their shareholders . . . . Ex post judicial enforcement of liability rules may be the sole recourse for those shareholders whose other linkages to management are insufficient to permit alternative forms of monitoring.”\footnote{Curtis J. Milhaupt, *A Relational Theory of Japanese Corporate Governance: Contract, Culture, and the Rule of Law*, 37 HARV. INT’L L.J. 3, 57 (1996).}

It seems unlikely that large corporate shareholders in close corporations with contractual ties to those corporations would not have sufficient linkages to management to permit monitoring. Two alternative explanations may help explain this new evidence of a high number of derivative suits in close corporations. First, the trend may be further indication of insiders’ ability to gain access to information in close corporations. Relational governance may be offset by the ability of shareholders in privately held corporations to obtain information on which to base a suit.
Second, perhaps by the time that litigation becomes the only option for a shareholder in a close corporation, relations are so embattled that only litigation can break the impasse. Because close corporations tend to be illiquid, most shareholder suits in close corporations in the United States are involuntary dissolution cases in which the minority is simply trying to get out. The Japanese Commercial Code (art. 406-2) provides relatively few criteria for court-ordered dissolution, a remedy that is only available if the company is at risk for “irreparable loss” or “grossly improper management,” and then only to ten-percent shareholders. Derivative suits in Japan may give minority shareholders a last litigious straw when relational governance fails and dissolution is unavailable or unwieldy.

IV. PRIVATE AND PUBLIC ENFORCEMENT

A final factor enters the calculus of plaintiffs and attorneys when deciding whether to bring suits: government enforcement, often in the form of criminal prosecution. In many cases, derivative suits “piggyback” on such enforcement actions. Although I discuss piggybacking separately in this Part for purposes of analysis, government enforcement actions are not a separate phenomenon, but an integral part of the calculus of plaintiffs and attorneys when deciding to bring suit.

Before the 1990s, shareholders wishing to sue faced an uphill battle in gathering information about defendants’ conduct. Information disclosure is not terribly abundant, shareholder rights to view corporate records are predicated on the holder having at least three percent of the shares, cause must be shown to appoint an outside inspector, and pretrial discovery

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is nonexistent. Before international competition crept into Japan, this sort of arrangement, in which directors had great leeway in decisionmaking, was socially acceptable and even considered by some to be good business practice. But with growing international competition, the system was difficult to sustain politically, socially, and economically.

In the early 1990s, after the bursting of the Japanese real estate and stock market bubble and with an influx of foreign business underway, prosecutors began aggressively to pursue individual wrongdoers in the corporate context. With increased criminal enforcement and public announcements of state-gathered evidence, potential shareholder-plaintiffs were able to gather more information about corporate activities, and specifically management misdeeds, than they had in the past. In effect, prosecutorial subpoena and investigative powers became a substitute for the lack of effective means of information gathering by shareholders.

Prosecutors became especially active in pursuing sokaiya rabble-rouser payment cases, securities violations, and, eventually, tainted-blood HIV cases. Not coincidentally, the derivative suits brought against directors of large public corporations tend to raise the same common issues: “securities scandals, the construction contracting industry (bribery and bid-rigging scandals), payments to sokaiya to keep corporate secrets, tainted-blood HIV cases, and other large corporate scandals.”

Once the prosecutors have obtained a guilty verdict, derivative suit settlement should be relatively easy: plaintiffs use evidence gathered by the state, defendants often cave, and the homogeneous Japanese professional judiciary is unlikely to reach

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86 See, e.g., Osamu Sakuma, *Kooporeeto Gabanansu to Keijihe* [Corporate Governance and Criminal Law], 1542 SHø11 HøMU 23 (1999). As Eric Feldman notes, the decision to prosecute in the HIV cases was spurred on by other civil actions. ERIC A. FELDMAN, THE RITUAL OF RIGHTS IN JAPAN: LAW, SOCIETY AND HEALTH POLICY 128 (2000).

a different verdict in a civil case. Because prosecutors have a 99.9% success rate, many plaintiffs simply initiate suit when the indictment is filed.

Increased prosecutorial action reduced the transaction costs to shareholders of identifying potential winning cases for derivative suits. Bringing a losing case can be quite expensive, as the plaintiff must pay the attorneys’ retainer and the defendants’ court costs. But bringing a winning case can reap a net profit, as the company will pay attorneys’ fees. If an attorney can identify a potential winner with some certainty, he may be more likely to forego the retainer. Prosecutors help attorneys and plaintiffs pick these potential winners and avoid lemons.

Perhaps the best empirical evidence of a causal relation between public and private enforcement is a direct examination of the cases. Of the 140 cases that I examined, I was able to identify 20 in which criminal penalties were imposed, 20 involving pending criminal cases, and another 13 in which the action in question was the subject of some sort of official investigation. In 50 of these 53 cases, criminal enforcement preceded civil enforcement. In the nine cases discussed in Part II in which plaintiffs recovered damages (one victory and eight settlements), all but one case involved criminal activity. In fact, because derivative litigation institutions are relatively weak in the absence of criminal wrongdoing, some commentators state – and my evidence at least suggests -- that plaintiffs may only be successful in cases in which prosecutors go forward. As a prominent attorney writes, “Because the courts as a general rule hold that even mistaken business judgments will not be questioned in the absence of illegal acts, in judicial

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88 See J. Mark Ramseyer & Eric B. Rasmusen, Why is the Japanese Conviction Rate so High?, unpublished manuscript.
cases involving listed companies, the only shareholders who have litigated successfully have been those whose directors committed illegal acts.”

It could be that the increase in public and private enforcement are both caused by the same phenomenon: increased managerial misdeeds during the bubble economy years. Although an increase in managerial misdeeds over the period may have occurred, I found that in practice, private action tends to follow prosecutorial action, and not the other way around. Civil suits are often filed immediately after the prosecutor indicts. As one attorney told me, “I would only bring an action if the prosecutors acted first. That gives me a good chance of winning; without it, I have a good chance only of losing.” The leading Japanese corporate law journal’s editorial department echoes these sentiments, stating that by 1999, “[i]t is becoming normal for parties to reach a settlement agreement after the defendants have been found guilty in a criminal proceeding – probably because after it’s clear that there is a violation of the law, it’s useless to fight.”

To attempt to examine empirically the relationship between prosecutorial action and derivative litigation on a broader scale, I compared the prosecution and judicial disposition of white-collar crimes in Japan with Japanese derivative litigation rates. Because there are no reliable categorical data on “white-collar crime,” I constructed two indexes using data on indictments and court cases. The Ministry of Justice publishes Annual Report of Statistics on Prosecution, which contains data on the number of criminal indictments by category. The

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89 Hideaki Kubori, Kachô Kurasu no Chikara o Ikaseru Nihonkei no Kigyô Tôji o Kangaeyô [Let’s Think about a Japanese-style Corporate Governance System that is Invigorated by the Power of Middle Management], 898 NIKKEI BUS. 43, 45 (July 7, 1997).

90 This fact may help explain why the filing of a derivative suits has little impact on stock returns, as the market may have already incorporated such information into the price.
Supreme Court General Secretariat similarly publishes *Annual Report of Judicial Statistics*, containing data on court cases. Using these sources, I examined data on indictments and court cases for three categories of offenses for the period 1988-1998: “civil” laws including the Commercial Code and the Bankruptcy Law, securities laws, and banking laws. The data are not comprehensive. They do not include, for instance, bribery of public officials or garden-variety embezzlement, which are covered by the Penal Code but are nevertheless crimes in which plaintiff-shareholders would be likely to have an interest. Still, they give a relatively accurate picture of the kinds of criminal actions in which shareholders normally would be interested and which are generally included in Japanese studies of white-collar crime:92 Commercial Code violations (including payments to sokaiya, special embezzlement, receipt or demand of a bribe, and excessive issuance of shares), securities fraud, and banking fraud.

The results can be quickly summarized. For almost every category of white-collar crime, both in terms of indictments and court cases, the 1993-1998 annual average figures are substantially higher than the 1988-1993 figures. The total figures for the post-1993 period are more than sixty percent higher for both indictments and court cases than the pre-1993 period.93

These broad data are quite crude. But while it is impossible to show a direct relationship between public and private enforcement rates, the general statistics are consistent with the theory and the direct evidence, as the derivative action increase correlates with increases in criminal indictments and court cases not only in each individual category, but across both broad white-
collar crime measures. The prosecution story is further supported by the fact that derivative litigation increased slightly even before the 1993 reduction of filing fees, while prosecution in that period rose as well.\textsuperscript{94}

There is nothing particularly Japanese about this private-public enforcement arrangement. In the United States, shareholder-plaintiffs commonly “piggyback” on SEC and antitrust enforcement actions in deciding whether to bring suit. According to John Coffee:

As an entrepreneur who is compensated only when successful, the plaintiff’s attorney bears the costs of failure and seeks to minimize those costs by free riding on the monitoring efforts of others. The classic illustration of this pattern is in the field of antitrust enforcement, where private antitrust class actions have tended to piggyback on a prior governmental proceeding (such as a grand jury indictment or a Federal Trade Commission proceeding).\textsuperscript{95}

Other examples abound: one study found that at least one-third of securities class actions followed SEC proceedings or bankruptcy filings;\textsuperscript{96} another found that the only successful insider trading private actions were those that followed SEC action.\textsuperscript{97}

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\textsuperscript{94} It may be possible for shareholder-plaintiffs to influence the system by encouraging criminal prosecution. According to the Code of Criminal Procedure, citizens may inform public prosecutors of crimes in two ways. Complaints (kokuso) are lodged by victims or their relatives. Code of Criminal Procedure 241. Accusations (kokuhatsu) are lodged by anyone who believes that there has been a criminal offense. Code of Criminal Procedure 239(1). Both have been filed in connection with derivative actions, further suggesting linkages between public and private prosecution. For kokuhatsu, see Nupis Hong Kong Ltd. V. Funatsu (Katakura Case), Tokyo District Court, 1395 HANREI JHO 144 (Judgment of Apr. 18, 1991); for kokuso, see Watanabe v. Asanuma (Asanuma Case), Osaka District Court, 924 Hanrei Times 258 (Judgment of Aug. 28, 1996).

\textsuperscript{95} Coffee, supra note 41, at 681.


\textsuperscript{97} See Michael Dooley, Enforcement of Insider Trading Restrictions, 66 VA. L. REV. 1, 16 & 16 n.82 (1980). The recent SEC policy of routinely seeking disgorgement may mitigate this phenomenon, as civil damages are limited by any disgorgement paid to the SEC. See 15 U.S.C. 78t-1(a) (1994).
In Japan, however, the calculus is slightly different than in the United States. Besides differences in attorney incentives and information markets, the role of derivative suits in the broader enforcement scheme adds perspective as to why so many cases -- over 1/3 of those that I examined -- appear to rely on prosecution. This broader enforcement scheme can be divided into two: derivative actions can enforce directors’ duties either before violations occur (ex ante) or after (ex post).

1. *Ex ante enforcement.* In her study of derivative litigation in the United States, Roberta Romano examined whether derivative litigation might function as a “substitute monitor” of managers. She concluded that the evidence was mixed. While there were no significant differences in board composition, firms with blocks of stock held by outsiders were more likely to be sued, and inside ownership is in firms with duty of loyalty claims was higher than that in firms with duty of care and federal law violation claims.

In Japan, corporate governance institutions might make derivative litigation a more useful (but still weak) monitoring device than in the United States. Because directors are largely insiders, monitoring by shareholders could be a more useful substitute for independence than in the United States. Japanese directors also seldom have more than trivial stockholdings (and before a 1995 Commercial Code amendment, stock options for managers were nonexistent). Because their incentives are arguably less aligned with those of shareholder than in the U.S., Japanese directors may have less incentive to self-police. Contrary to stories of efficient *keiretsu* and main bank monitoring, many of the firms experiencing derivative litigation are affiliated with a large corporate group. And contrary to legends of Japan, Inc., monitoring in the form of

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98 Romano, *supra* note 2, at 80.
bureaucratic oversight is often lacking.\textsuperscript{99} In such an environment, derivative litigation could potentially be more useful in Japan than in the United States.\textsuperscript{100}

To some extent – and measurement here is extraordinarily difficult -- shareholder litigation appears to deter some objectionable director conduct. Curiously, it appears to have done so in many large public corporations by shifting the internal balance of power away from managers to members of internal legal departments. Although members of legal departments are usually not lawyers, they usually have law training (both formal and practical), and are usually the best-suited persons in the company to give advice pertaining to derivative liability. As managers seek to avoid liability, they increasingly appear to be turning to in-house legal specialists for advice. This shift of power enables legal departments (and often their professional legal advisors) more closely to monitor management activity, and, if nothing else, to control the flow of some egregiously bad ideas.\textsuperscript{101}

2. \textit{Ex post enforcement}. Economists suggest that optimal enforcement combines high sanctions with low enforcement rates.\textsuperscript{102} Sanctions may include civil fines, criminal punishment in the form of fines or imprisonment, and reputational penalties. Consider the latter two factors in the Japanese derivative litigation context. First, lax criminal punishment in Japan is an often-mentioned feature of the Japanese system, which sends fewer than 1 in 1,000 offenders to prison


\textsuperscript{100} The efficiency of the power shift, of course, depends on a balance of liability concerns with business concerns. Japanese corporations are historically risk averse, see Curtis J. Milhaupt, \textit{The Market for Innovation in the United States in Japan: Venture Capital and the Comparative Corporate Governance Debate}, 91 NW. U. L. REV. 865, 892-94 (1997), and giving legal professionals greater control over managerial decisions may not necessarily be the best business course.

\textsuperscript{101} See KUBORI ET AL., supra note 19, at 213; see also Donald C. Langevoort, \textit{The Epistemology of Corporate-Securities Lawyering: Beliefs, Biases, and Organizational Behavior}, 63 BROOK. L. REV. 629 (1997).

for more than five years, and only five percent of its suspects to prison at all.103 The low level of actual punishment is especially clear in the Japanese white-collar crime context. In my 1999 study of sokaiya payments, a crime punishable by up to three years imprisonment, no executive from any of the thirty-three firms that had been sentenced received actual jail time.104

Perhaps the lack of punishment by imprisonment reflects differing forms of punishment in Japan. In Japanese culture, we are sometimes told, shame and social controls substitute for traditional forms of punishment.105 But shame and social controls are often weak. Survey data suggest that “Japanese can be expected to recommend sanctions that restore the status quo to a greater extent than Americans across all types of relationships.”106 In the derivative suit context, longstanding corporate practice in Japan dictates that corporate executives who are punished, even criminally, for actions taken on behalf of the “company” (management and employees) such as payments to sokaiya, are not heavily punished with social controls, and in some cases are rewarded. Anecdotal evidence of the practice is easy to find. Often directors resign in “disgrace” simply to receive lucrative retirement benefits or to receive a transfer to a subsidiary’s


104 West, supra note 62, at 777. Cf. John R. Emshwiller & Michael Schroeder, Stock-Fraud Cases Sometimes Lose Their Sting, WALL ST. J., June 27, 2000, at C1 (of 22 sentenced in 1996 U.S. federal white-collar crime cases, half received no prison time, and half received prison sentences ranging from three to 71 months).


106 V. LEE HAMILTON & JOSEPH SANDERS, EVERYDAY JUSTICE: RESPONSIBILITY AND THE INDIVIDUAL IN JAPAN AND THE UNITED STATES 137 (1992). In 1993, Joseph Sanders, Lee Hamilton, and Toshiyuki Yuasa conducted surveys in Tokyo, Washington, and Moscow in which they read four “vignettes” of worker mistakes and white-collar crime and asked for respondents’ reactions as to what sort of sanctions should be imposed. In response to each vignette, more than one-third of Japanese respondents thought that “restoration” was the appropriate sanction, while no vignette in the other two countries gained more than 10% support for such measures. An average of five percent of Japanese respondents thought that the perpetrator should be fired, compared to 25% for Moscow and 27% for Washington. See Joseph Sanders et al., The Institutionalization of Sanctions for Wrongdoing inside Organizations: Public Judgments in Japan, Russia, and the United States, 32 LAW & SOCIETY REV. 871 (1998).
board, as was the case in 1998 at three securities houses and two Mitsubishi affiliates.\textsuperscript{107} In some cases, as with Nomura Securities in 1995, directors who resign to take responsibility for scandal simply return to the board after brief periods of “rehabilitation.”\textsuperscript{108}

Caution should be exercised in evaluating such data, as it may reflect institutional approaches to dispute resolution as much as it is reflective of some notion of “culture.” But whatever the cause, the data do suggest that the expected non-legal sanction in Japan is more likely to be restoration than termination. While the practice of restoration and reward appears to be gradually changing in response to shareholder activism (and derivative suits),\textsuperscript{109} it appears that in the elite white-collar crime setting, non-legal sanctions against directors do not substitute for legally mandated punishment.

Another possible source of enforcement is capital markets. Firms in Japan might experience a market-based sanction, as appears to occur in the United States when companies commit fraud.\textsuperscript{110} One question in the derivative suit context is to what extent reputational sanctions against firms deter managerial misbehavior. Again, while the situation may be changing, the reputational sanction to individual directors in Japan whose firms commit fraud historically appears relatively weak. Trivial stockholdings by directors further suggest that market-based sanctions might have less impact on Japanese directors than their U.S. counterparts.

\textsuperscript{107} See Mitsui Against Pensions for Scandal-hit Execs, JAPAN ECONOMIC NEWswire, June 24, 1998.


\textsuperscript{109} See Mitsui Against Pensions for Scandal-hit Execs, JAPAN ECONOMIC NEWSwire, June 24, 1998 (Mitsui Trust opposes retirement bonuses); Kaigai Toshika no Hantaih\textsuperscript{\ua{30}} Ky\textsuperscript{\ua{5}}z\textsuperscript{\ua{4}}ka [Will Foreign Investor No Votes Increase?], NIHON KEIZAI SHINBUN, June 19, 1998, at 12.

\textsuperscript{110} Jonathan M. Karpoff & John R. Lott, Jr., The Reputational Penalty Firms Bear from Committing Criminal Fraud, 36 J. L. & ECON. 757 (1993).
Given this state of sanctioning institutions, the practice of using private actors to enforce public policy through derivative suits may not be entirely unappealing. There may be problems associated with the assigning to private actors the absolute right to enforce public policy, or the blurring of lines between criminal and civil liability. But because criminal and social sanctions are weak, additional private sanctions – piggybacked on public ones -- may be useful in achieving heightened deterrence. If not deterrence, derivative suits at least achieve disgorgement of profits, and sometimes disgorgement in excess of insurance coverage. An additional private sanction in the form of derivative suit damages thus may function more as a public good in Japan than in the U.S. enforcement regime.

The efficacy of the system if far from certain. It is unclear, for instance whether any general deterrence can be gained from a system that appears – if stock price evidence, success rates, and continued scandal are any guide-- to create little specific deterrence. If the derivative suit mechanism in Japan continues to produce few winning cases, it would seem not to be the most appropriate basis for a broad corporate crime enforcement strategy. Still, if directors who commit criminal acts continue to lose, the system could conceivably evolve into one in which meritorious suits based on criminal conduct far outnumber strike suits. Even without deterrence gains, the system might also be marginally effective in correcting some individual egregious cases in which directors profit at shareholder expense.

CONCLUSION

Determining the precise goals of a diverse and unrelated body of plaintiffs with multiple motivations is impossible. But through careful analysis of post-1993 shareholder derivative suits against large public corporations in Japan, some general conclusions can be drawn. First, shareholders appear to receive few gains from derivative litigation. Most suits are losers – in my sample of Tokyo Stock Exchange firms, only one plaintiff won (another winner is on appeal), while one-third lost outright, and another quarter were doomed by adverse bond motion rulings. Few cases settle (17.6% in my limited sample), suggesting, at least, that shareholders in Japan have even less reason than shareholders in the U.S. to bring suit. Even the winners do not result in increases in shareholder wealth. In a few cases, some plaintiffs receive individual awards as kickbacks from attorneys’ fees, but the prevalence of this practice is unknown.

Second, attorney’s fees, even in a system with very different fee structures than those of the United States, appear to drive most shareholder litigation in Japan. Japanese attorneys can profit based on the cartel’s up-front retainer provisions. Although other work may ultimately be less risky and more profitable under the fee rules, attorneys in a large number of cases are able to use collective action to spread the risk of loss among several attorneys. Some attorneys may pursue derivative suits even in the absence of large monetary rewards, but these attorneys often receive gains in the form of advertising (which is otherwise prohibited by law), rewarding work, or altruistic gains.

Third, some additional factors are helpful in explaining cases. Plaintiffs and attorneys typically have multiple motivations, and a residuum of anger, spite, altruism, fairness, and justice appears in Japan as elsewhere. Sokaiya rabble-rousers sometimes bring losing suits to harass

Public Programs and Private Rights, 95 Harv. L. Rev. 1193 (1982) (discussing situations in which courts are
managers into paying blackmail. Although evidence is unclear, moral hazard suggests that some suits may be made more likely by the existence of D&O insurance. And some suits in close corporations may reflect the above factors as well as more basic internal disagreements and dissolution problems.

Finally, public enforcement institutions help plaintiffs and attorneys avoid lemons. To find winning cases, plaintiffs and their attorneys initiate suit against indicted managers. The civil enforcement system may supplement weak white-collar criminal and social sanctions.

Beyond attorney incentives, determining an exact breakdown of which motivations matter most is difficult, and of course many cases have multiple motivations, but again, some general numbers can be drawn from my study of 140 total suits. Fifty-three were linked in one way or another to criminal wrongdoing. Ten cases involved sokaiya or similar actors. Forty-eight were against privately held corporations. It is impossible to determine the exact number of cases in which (1) non-monetary factors, (2) insurance, and (3) secret deals played predominant roles.

The Japanese experience suggests at least two implications for derivative litigation in the United States and elsewhere. First, the Japanese event study data generally follow the event study results for U.S. data that show no significant shareholder wealth increases from derivative litigation. These findings are consistent with the theory that derivative suits in general do not result in direct shareholder wealth increases.

Second, while Roberta Romano found in her study of the U.S. system that “[t]he principal beneficiaries of the litigation [] appear to be attorneys, who win fee awards in 90
percent of settled suits,”¹¹² the smaller awards in Japan relative to other cases and the relative lack of settlements suggest that derivative litigation will occur with relative frequency even without the level of monetary incentives seen in the United States. As long as some attorneys have some incentive to bring suit (whether because of paying clients, fees, fame, or altruism), derivative litigation may persist. More broadly, the similarity of the Japanese evidence to that of the United States suggests that some criticism of the derivative suit mechanism may be misplaced. Derivative suits in the United States persist not because of a litigious society or an overpopulation of overpaid attorneys, but because of the incentives created by the mechanism itself.

Former Japanese Supreme Court Justice Yasukazu Kagawa has stated, “I don’t think that derivative suits are ‘Japanese.’ The fact that shareholders’ derivative suits are supposed to improve the corporation or correct management misbehavior just doesn’t seem right. . . . Derivative suits sell newspapers, but most of the suits turned down by the courts are just nuisance suits . . . we can’t say that all of these suits are serious. Why is that? Because this system just doesn’t suit Japan.”¹¹³ Perhaps. But the findings of this Article suggest that if it doesn’t suit Japan, it probably doesn’t for the same reasons that it doesn’t suit the United States – its primary beneficiaries are not suing shareholders, but attorneys.

¹¹² Romano, supra note 2, at 84.