

Recharacterisation of product risks

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Introduction

In Japan, product-related risks have typically been considered in the context of defects or safety, and product liability has commonly been the main product-related concern for manufacturers. However, in reality, Japan has significantly fewer product liability cases than other industrialised countries. Further, the product liability awards rendered by the Japanese courts tend to be considerably lower than those issued by, for example, the US courts. In this context, businesses may not consider product liability to be a top risk priority.

Product recall risk has also been one of the main product-related concerns for manufacturers. This is not only because product recall procedures (particularly global procedures) can be costly and have a significant financial impact on manufacturers, but also because such procedures can damage a company's reputation if handled improperly. However, regardless of whether a risk is product liability or product recall related, the general view is that product safety is a key concern.

Although product compliance has always been an important issue for manufacturers, it has historically been overshadowed by safety-related product risks, and considerations regarding product compliance have typically been integrated with other product risks. However, manufacturers' awareness of the risks associated with product compliance has grown and product compliance has now become a top priority. The catalyst for this shift in attitude was a recent spate of data falsification cases.

Data falsification incidents

As a reaction to the recent spate of data falsification cases, in December 2017 the chair of the Keidanren (also known as the Japan Business Federation) – whose members include more than 1,300 representative companies and over 100 nationwide industrial associations – asked member companies to voluntarily undertake investigations into product quality control and to report on and publicise any incidents of falsification. Since then, many Japanese companies have carried out internal investigations or asked external specialists to do so, and a surprising number of companies have discovered incidents of data falsifications or manipulation or other fraudulent activities in relation to product inspections at their manufacturing sites. This trend looks set to continue. In most cases, the fraudulent acts or practices:

- continued over a long period;
- were carried out on an organisation-wide scale; and
- involved a large number of products or types of product.

The impact of quality-related incidents on affected companies has been significant.

Companies affected by quality-related incidents may have to recall the product and will also likely be exposed to liability to their business partners due to breaches of contract or indemnification, among other things. Further, depending on the factual background, such companies may face criminal liabilities. In addition, because quality-related incidents signal an ineffective corporate compliance programme and poorly functioning governance, an investigation into such problems will inevitably reveal managerial problems, regardless of whether any safety concerns arise as a consequence of the incident. Thus, based on the recent spate of quality-related incidents, senior management, directors and company boards now see product compliance as a major business risk area.

Further, as was the case with the Keidanren member companies' investigations, the findings of most data falsification cases in Japan are summarised in a public report, regardless of whether a safety-related incident occurred. The Japanese civil litigation system has no equivalent to discovery, as provided for by, for example, the US civil procedure rules. As a general rule, the party bearing the burden of proof will present its case by selectively referencing evidence that is favourable to its case. However, because the results of quality-related incident investigations are made public, even without discovery, plaintiff attorneys can obtain detailed information relating to the incident from the defendant companies. Accordingly, the potential litigation risk that a company which has engaged in data falsification faces is far greater than in the past. Further, the publication of a detailed report in Japan may lead to a waiver of the attorney-client privilege held by a reporting company in other jurisdictions where such privilege is recognised.

Comment

Due to the recent spate of quality-related incidents, product-related risks have been recharacterised and many manufacturers now view product compliance, which was previously overshadowed by product liability and recall concerns, as a major business risk area. The prevention of data falsification is tied to a new awareness among manufacturers of the importance of compliance when launching a new product. Further, the Japanese authorities are closely scrutinising manufacturers' product compliance.

For further information on this topic please contact Junichi Ikeda at Nagashima Ohno & Tsunematsu by telephone (+81 3 6889 7000) or email (junichi_ikeda@noandt.com). The Nagashima Ohno & Tsunematsu website can be accessed at www.noandt.com.

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Junichi Ikeda