THE STANDARDS OF JUDGMENT FOR DISPUTE RESOLUTION IN FINANCIAL ADR OF JAPAN

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Abstract

Japan's modern financial alternative dispute resolution (ADR) system was established by a series of revisions to 17 separate financial and banking statutes. While the revisions established a system in which financial disputes could be heard, they were notably silent on the *standards for judgment*. This article seeks to extrapolate those standards. First, this article looks towards the standards of judgment used for *general* ADR. I begin by establishing the historical context of ADR in Japan, followed by analyzing Japan's modern ADR laws. I describe, in detail, key provisions from the ADR Promotion Act, the Civil Conciliation Act, and the Arbitration Act, with a particular focus on the requirements for "rule of law." Second, I analyze the financial ADR laws of the United Kingdom and how the courts have interpreted standards of judgment for those laws. Third, I attempt to extrapolate standards of judgment for financial ADR in Japan by looking towards the "purpose" provisions of the various financial / banking laws. I analyze the purpose of the financial ADR system in light of the needs of disputing parties and with a view towards the underlying administrative goals of the government agencies responsible for the supervision of financial service providers. I further apply, by analogy, the key provisions of the Civil Conciliation Act to further refine my interpretation. I conclude that there are no rigid standards. Rather, judgments ought to be made in accordance with the "fair and reasonable (*Jori*)," which is a reflection of the "common sense" prevailing in society or "good sense" prevailing in the relevant financial service industries. In addition, judgments should be made with the aim towards maintaining the public's trust in financial services. Insofar as these standards are satisfied, judgments can depart from application of statutory laws or court precedents. In light of these extrapolations, this article concludes with a checklist of requirements for financial ADR judgments. These checklists are a combination of the positive and negative requirements extrapolated from relevant ADR laws, the purpose of the financial / banking laws, and the needs for disputing parties.

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I. INTRODUCTION

A. The Principal Issues Examined in this Article

The alternative dispute resolution ("ADR") method used by Japan's financial ADR system is conciliation. The "special conciliation proposal" is presented to disputing parties as a conclusive proposal, and is legally binding (but subject to certain limitations) on the financial service provider who is a party to the dispute. We therefore expect that the accumulation of "special conciliation proposals" shape principles, which affect the manner of how financial services are provided in Japan. In that sense, the "special conciliation proposal" is not just a settlement proposal for the disputing parties to accept, but has significance as a *judgment* rendered by the financial ADR system in Japan. Thus, the standards of judgment for the Japan's financial ADR deserve careful examination in this article. In considering the standards for financial ADR in Japan, I will focus on conciliation and mediation standards, but the standards for arbitral awards, which bring about the final remedy for most disputes, will also be taken into consideration.

It may be too ambitious and unfruitful to attempt to clarify the standards of judgment for ADR, as the decisive factor in ADR is often "trust" in the "third party" selected to resolve the disputes. The decisive factor may be who heard the parties' claims and proposed the direction to resolve the dispute rather than how laws were interpreted and applied. Since ADR results have not been disclosed and publicized in the main street of history, it is not necessarily clear what has played the pivotal role in the history of ADR. It may have been "persons of high caliber" who were highly esteemed in the respective societies. This may hold true even today.

At this time, the financial ADR system has only recently been established and has just begun operations in Japan. Nevertheless, this article attempts to clarify as much as possible the standards of judgment that should be applied to financial ADR.

Positioned between the judiciary and administrative organs of government, financial ADR has the role of providing individual protection to customers of the financial service industry and establishing sound industry practices by helping administrative authorities regulate and supervise the financial service industry. What should be the standards of judgment for financial ADR in light of such position and role?

How should a court treat a "special conciliation proposal" presented by an adjudicator if one of the parties does not accept such proposal and thereafter brings a suit in court for the same claim? The court could examine the claim as a new lawsuit as it normally would without considering the special conciliation proposal. However, the court could also recognize that the special conciliation proposal reflects the expertise of the financial service industries and take that into consideration in one way or another. If the latter position is taken, how should the court consider the special conciliation proposal and what standards of judgment will the court require of it?

It is needless to say that the Civil Code, the Commercial Code, the financial service industry laws, and other statutes of Japan and various

regulations thereunder provide standards of judgment for dispute resolution in financial ADR of Japan. It is the aim of this article to articulate such standards of judgment and describe how these standards should be further applied in financial ADR based on the result of applying such statutes and regulations. I conclude financial ADR should not be based upon personal reliance on adjudicators. Rather, the legitimacy of such standards of judgment is necessary for society to accept financial ADR as a valid dispute resolution system. Neutrality or fairness of the dispute resolution institutions is not enough.

B. Brief Summary of this Article

This article will examine whether the standards of judgment for dispute resolution in financial ADR should be bound by the application of statutory law and judicial precedents. I conclude that the decisions for dispute resolutions in financial ADR should be made using "good sense" with a view towards satisfying the purpose of the financial ADR system and, as such, the decisions may depart from the application of statutory laws or judicial precedents. This conclusion is supported by Japanese law. I expect that the accumulation of precedents in financial ADR will facilitate the development of law applicable to the financial service industry.

Section II outlines the establishment of Japan's financial ADR system and dispute resolution procedures. Currently, there are no provisions of any laws articulating the standards of judgment for financial ADR.

Next, in the absence of statutory provisions on such standards of judgment, Section III examines *general* ADR under Japanese law with a view to extracting the standards of judgment for *financial* ADR. The dispute resolution standards of the Civil Conciliation, as stipulated in the relevant Japanese statute, are "reasonable and appropriate to the actual conditions."[1] As to the recognition of foreign arbitral awards, Japanese law accepts the standards applied in foreign ADR insofar as such arbitral awards are not contrary to the public order and good morals of Japan.[2] While ADR must satisfy the "Rule of Law" requirement, the modern principles of "Rule of Law" give a wide range of freedom as to the standards of judgment for ADR.

Section IV examines the standards of judgment for financial ADR of the United Kingdom by looking into a UK court decision. The United Kingdom adopted financial ADR systems prior to Japan. The Financial Services and Markets Act of 2000 adopted in the UK provides that the ombudsman, who presides over the financial ADR procedure and renders the final judgment, is authorized to make decisions by reference to what is, in the opinion of the

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[1] Minji chōteihō (民事調停法) [Civil Conciliation Act], Act No. 222 of 1951, art. 1 (amended 2011), *available at* http://law.e-gov.go.jp/htmldata/S26/S26HO222.html.

[2] Chūsaihō (仲裁法) [Arbitration Act], Act. No. 138 of 2003, arts. 45-1-45-2 (amended 2004), *available at* http://law.e-gov.go.jp/htmldata/H15/H15HO138.html.

ombudsman, "fair and reasonable" in light of all the circumstances of the case.[3] According to court precedents in the UK, this means that an ombudsman may be subjective in his or her judgment unless such judgment is "perverse or irrational."[4]

After examining *general* ADR in Japan and the UK law concerning its financial ADR system, Section V examines the standards of judgment for dispute resolution in Japan's *financial* ADR system. First, I explain the purpose of financial ADR in the laws governing financial service industries that are subject to the financial ADR system. The purpose of the financial ADR can be summarized as "giving due regard to the public nature of financial services, to ensure sound and proper business operations, to develop fair pricing by ensuring fair dealing, to maintain the public's trust of financial service industry, and to provide customer protection." Second, I examine unique features of financial products and financial services, as well as the special status of their financial ADR system, including its function as an infrastructure for the financial system. Third, I examine demands on the financial ADR standards from both the disputing parties as well as the regulators on financial service providers. Fourth, based on the aforementioned standards of judgment for the *general* ADR under Japanese law, I summarize the sources of law that should either be applied or be applied *by analogy* to the standards of judgment for financial ADR. Fifth, I summarize guiding principles that determine the standards of judgment for the financial ADR system, focusing on the need for dispute resolution which prompted the establishment of the financial ADR system. Sixth, I conclude that "the decisions for dispute resolutions in the financial ADR should be made by good sense with a view to satisfying the purposes of the financial ADR and the decisions as such may depart from the result of applying statutory laws or judicial precedents."

Finally, in section VI, I put together checklists for making decisions in the financial ADR and present challenges for further examination and consideration of the Japan's financial ADR.

II. DISPUTE RESOLUTION PROCEDURES IN THE FINANCIAL ADR SYSTEM OF JAPAN

A. Establishment of the Financial ADR System in Japan

The financial ADR system began in Japan with the enactment of the 2009 partial revisions of the Financial Instruments and Exchange Act and other relevant acts ("Financial ADR System Founding Laws").[5] Disputes began to be

[3] Financial Services and Markets Act, 2000, c. 8, § 228(2) (U.K.), *available at* http://www.legislation.gov.uk/ukpga/2000/8/pdfs/ukpga_20000008_en.pdf.

[4] *Heather Moor & Edgecomb Ltd., R v. Financial Ombudsman Service & Anor*, [2008] EWCA Civ. 642, [19] (appeal taken from Eng.).

[5] The 2009 partial revisions amended 17 different financial industry laws. The amended laws are the Financial Instruments and Exchange Act, the Mutual Loan Business Act,

resolved via financial ADR on October 1, 2010. The financial ADR system here refers to a system that provides solutions for customers' complaints against financial service providers and resolves conflicts between customers and financial service providers through ADR procedures by designated dispute resolution institutions instead of judicial procedures. Designated dispute resolution institutions are officially designated by the Prime Minister under the Financial Instruments and Exchange Act ("FIEA") and other relevant financial service industry laws, as the case may be.[6] Recent developments in two fields of Japanese law precede the establishment of this system.

First is the increasing importance of ADR within Japanese society. When we look at dispute resolution in Japan after the 1950s, trials by courts or settlement and conciliation with assistance by courts were widely accepted and people did not recognize the necessity for any other ADR system for resolving disputes. Since 2000, however, people have gradually began to recognize that a system for resolving disputes without involvement of courts should be emphasized, partly because the burden on courts was growing and the number of disputes requiring specialized expertise has increased. This led to the enactment of Arbitration Act of 2003 (later amended in 2004)[7] and the Act on Promotion of Use of Alternative Dispute Resolution of 2004 (later amended in 2011) ("ADR Promotion Act").[8]

Second is the growing demand for consumer protection. In 2004, the Consumer Protection Fundamental Act was revised and came to be known as the Consumer Basic Act. Acknowledging the gap between consumers and providers with respect to the quality and quantity of information as well as negotiating power, the Consumer Basic Act requires the national government,

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the Act on Concurrent Operation, etc. of Trust Business by Financial Institutions, the Agricultural Cooperatives Act, the Fisheries Cooperative Associations Act, the Small and Medium-Sized Enterprise Cooperatives Act, the Shinkin Bank Act, the Long-Term Credit Bank Act, the Labor Bank Act, the Banking Act, the Money Lending Business Act, the Insurance Business Act, the Norinchukin Bank Act, the Trust Business Act, the Shoko Chukin Bank Act, the Settlement Act, and the Act on Regulation, etc. of Mortgage Securities Business which was abolished by the Act for Developing Relevant Acts enacted with the Act of Partial Revision of Securities and Exchange Act, etc. Prior to the creation of this financial ADR system, certain industry associations, such as banks, securities firms and insurance companies, had their own voluntary complaint handling or ADR organs.

[6] *See, e.g.*, Kinyū shōhin torihikihō (金融商品取引法) [Financial Instruments and Exchange Act], Act No. 25 of 1948, art. 37-7 (amended 2012), *available at* http://law.e-gov.go.jp/htmldata/S23/S23HO025.html.

[7] Arbitration Act, *supra* note 2.

[8] Saibangai funsō kaiketsu tetsuzuki no riyou no sokushin ni kan suru houritsu (裁判外紛争解決手続の利用の促進に関する法律) [Act on Promotion of Use of Alternative Dispute Resolution], Act No. 151 of 2004 (amended 2011) [hereinafter ADR Promotion Act], *available at* http://law.e-gov.go.jp/htmldata/H16/H16HO151.html.

local governments, and industries to recognize the consumers' "right" to be properly and immediately relieved from any damage.[9]

It should be noted that settling disputes by litigation normally requires substantial resources and time. Thus remedying a complaint for a small claim through litigation is difficult. Some have complained that applying laws through judicial procedures and trials have left such complaints out of the judicial system. The financial ADR system is an attempt to resolve this problem by providing easy and immediate "relief" to customers, by use of a cheaper alternative scheme conducted out of courts.

B. Dispute Resolution Procedures Adopted for Financial ADR

As stipulated in the law, financial service providers each have the obligation to construct a basic contract that implements the financial ADR system with one of the dispute resolution institutions designated by the Prime Minister[10] and to comply with the procedures of complaint handling or dispute resolution initiated by the designated dispute resolution institutions or its adjudicators in accordance with the said basic contract, unless there is a reasonable reason not to comply.[11] In addition, they generally have the obligation to accept the "special conciliation proposal" presented to the disputing parties.[12] The "special conciliation proposal" is binding upon financial service providers as presented, with certain exceptions, but not on customers. In arbitration under the Arbitration Act, which also resolves disputes out of courts, an arbitrator is selected by agreement between the parties and an arbitral decision is binding upon both the parties involved.[13] The financial ADR system differs from arbitration in this respect.

The financial ADR process consists of three phases: (a) the claim handling phase, (b) the mediation phase, which creates the settlement proposal to be recommended for acceptance, and (c) the conciliation phase, which creates a "special conciliation proposal" to be presented to the parties with the decision's reasoning. The roles of the adjudicators and the purpose or contents of their decisions differ in each phase.

1. Complaint Handling Phase

In this phase, financial service providers are asked to respond to customer inquiries or complaints immediately with a thorough explanation. At this

[9] Shōhisha kihonhō (消費者基本法) [Consumer Basic Act], Act. No. 78 of 1968, arts. 1–2, 5 (amended 2012), *available at* http://law.e-gov.go.jp/htmldata/S43/S43HO078.html.

[10] Financial Instruments and Exchange Act, *supra* note 6, art. 37-7.

[11] *Id.* art. 156-44(2)(2).

[12] *Id.* arts. 156-44(2)(5)–156-44(2)(6).

[13] Arbitration Act, *supra* note 2, art. 45.

stage, it is important to hear the facts which may be important for future dispute resolution and record them accurately. In some cases, there may be further inquiries into the financial service providers and based on such inquiry, further explanation may be provided to customers. It is also necessary to investigate complaint handling measures taken by financial service providers. Filings for dispute resolution at designated dispute resolution institutions commence as early as this point.

At this stage nothing material will be decided upon by the staff of dispute resolution institutions independently. Nonetheless their responses and explanations to customers will be given in accordance to the policies of the relevant dispute resolution institutions, as well as the accumulated decisions of cases similar to the one before the staff. Therefore, educating the staff on such accumulated decisions is very important.

2. Mediation Phase

This procedure is undertaken by the adjudicator and falls under the category of "mediation of settlement" as stipulated in the ADR Promotion Act and is included in the definition of "alternative dispute resolution" as defined by the said Act.[14] This is a so-called "*Cho-tei*" in the Japanese language, and is equivalent or similar to "mediation" or "conciliation" in the English language.

3. Conciliation Phase

The special conciliation proposal is binding upon the financial service providers (subject to the limitations set forth below), but not on the consumer. The binding effect on the financial service providers is subject to their right to bring a lawsuit before the court in a limited period of time after the customer's acceptance of the proposal. Thus, all of the parties involved can request a court to hear the claim underlying the dispute.[15] Although different from an arbitral award, the standards for judgment used by the adjudicators in special conciliation procedures should, due to its binding force on financial service providers, be understood as closer to the standards applied in arbitration than the standards in the Mediation Phase as discussed in (2) above.

C. The Significant Impact of Standards for Dispute Resolution in the Financial ADR

In the Mediation Phase the adjudicator creates a settlement proposal and recommends that the parties accept it. The parties are not bound to accept it,

[14] ADR Promotion Act, *supra* note 8, art. 2(1).

[15] *Id.* arts. 2(6)(1)–(2).

but the settlement proposal is expected to be consistent, in essence, with the "special conciliation proposal," which will be presented in the Conciliation Phase if the settlement proposal is not accepted. For this reason, the parties will have great incentive to accept the settlement proposal. Thus, the rules for the "special conciliation proposal" guide the standards for the whole process of complaint handling and dispute settlement of the financial ADR institutions.

The standards of judgment for the "special conciliation proposal" will not only be the standards guiding the whole process of complaint handling and dispute settlement of the financial ADR institutions, but may also contribute to development of the law concerning the financial service industry. Both financial service providers and customers who are parties to the dispute can file a lawsuit asking for court's decision in lieu of accepting the "special conciliation proposal." In the event that the parties file a lawsuit, Japanese law does not require that the court "review" the special conciliation proposal offered by the adjudicator. A court may review the claim with a blank slate and act independently from the preceding dispute resolution procedures taken by the financial ADR institutions. Nevertheless, the "special conciliation proposal" offered in the ADR process still has a significant impact on judicial decisions because such proposal should reflect specialized expertise concerning the financial industry and should have been made with the aim towards realizing the administrative purpose of the financial ADR system. Thus, subject to and with the approval of court, the standards for "special conciliation proposal" could also contribute to the development of law with respect to the financial service industry.

D. Lack of Standards for Financial ADR in the Financial ADR System Formation Laws

1. Lack of Stipulations on the Standards in the FIEA and Other Financial Service Industry Laws

In the FIEA and other financial service industry laws which form the basis of financial ADR, there are no general provisions stipulating the standards of judgment for financial ADR. The financial ADR system was introduced in Japan by the "Financial ADR System Founding Laws," which amended each of the financial service industry laws. The "Purpose" provisions (Article 1) of each of the laws, however, were not revised. A series of provisions concerning the "designated dispute resolution institutions" were added to each financial service industry law, but no provisions were added to stipulate the purpose and principles of the financial ADR system nor were the standards for designated dispute resolution institutions or their adjudicators making decisions to resolve financial disputes provided.

The FIEA, Article 156-44, Paragraph 2, Item 5 stipulates the requirements for making the "special conciliation proposal."[16] In addition, as in the case of

[16] Financial Instruments and Exchange Act, *supra* note 6, art. 156-44(2)(5).

Article 6, Item 5 of the ADR Promotion Act,[17] Article 156-44, Paragraph 4, Item 4 of the FIEA requires, in providing the operating standards of designated dispute resolution institutions, that legal counsel shall be retained if specialized expertise is needed for the interpretation and application of law.[18] But there is no provision regarding how this measure should function in making judgments.

The general purpose of the financial ADR system must be inferred completely from the "Purpose" provisions of each of the financial service industry laws. In the Financial ADR System Founding Laws, there are no provisions on the concrete purpose and principles of the financial ADR system as well as the scope of the authority and discretion given to the designated dispute resolution institutions or their adjudicators or the standards of their judgment. These matters are also subject to interpretation.

2. The Legislative Intent of the Financial ADR System Founding Law

In the legislative process of the Financial ADR System Founding Law, what standards of judgment were thought to be desirable for dispute resolution in financial ADR?

There was no reference to the standards of judgment for dispute resolution in financial ADR in the government's reasons for the proposing the Financial ADR System Founding Laws, nor in the supplementary resolutions adopted at the time of passing the said bill on April 22, 2009 by the Financial Committee of the House of Representatives, and on June 16, 2009 by the Financial Committee of the House of Councilors.

3. Assignment Relating to the Standards for Dispute Resolution in the Financial ADR

It is an urgent issue for the adjudicator to decide the standards of judgment in the financial ADR process. With respect to whether or when to present the "special conciliation proposal," the FIEA provides that "when there is no possibility of reaching a settlement between the parties by the recommendation to accept a settlement proposal and if it is considered as suitable in light of the nature of case, the parties' intention, the parties' conduct in the procedures, and any other circumstances, the adjudicator can, with a view to resolving the dispute, create a special conciliation proposal and present it to the parties with reasons,"[19] but the FIEA, like all other laws formulating the financial ADR system, is silent as to how substance of the special conciliation proposal should be determined. It could be said that what

[17] ADR Promotion Act, *supra* note 8, art. 6(5).

[18] Financial Instruments and Exchange Act, *supra* note 6, art. 156-44(4)(4).

[19] *Id.* art. 156-44(2)(5).

is "necessary for dispute resolution" is a substantive requirement, but the Act provides no guidelines at all.

As the FIEA provides no clear standards of judgment, the adjudicators must decide standards of judgment by themselves. When the designated dispute resolution institutions try to set up, what criteria should be applied in their regulations on business operations, and what standards of judgment should be used by the adjudicators creating a "settlement proposal" in the Mediation Phase or "special conciliation proposal" in the Conciliation Phase? We must clarify the applicable standards by reviewing the standards of judgment for *general* ADR, considering the purpose of the financial ADR system, and looking at the accumulated financial ADR practices.

III. THE STANDARDS OF JUDGMENT FOR ADR IN GENERAL

The dispute resolution process for financial ADR is one of the procedures to resolve civil disputes between private parties with the involvement of a third party but without the litigation process. Such procedures are called "Alternative Dispute Resolutions" (ADR) as distinguished from the procedure to resolve disputes by courts in accordance with the litigation process. The Japanese courts are authorized to be such third parties in ADR. ADR conducted with the involvement of Japanese courts are called "Settlement before the Court" and "Conciliation." As stated in Section II above, the laws which established the financial ADR system do not stipulate standards of judgment for dispute resolution in financial ADR. Since financial ADR is a form of ADR, I will first examine the standards of judgment adopted for ADR in general, and then would like to clarify, on the basis of such standards for ADR in general, the standards of judgment which should be applied to the financial ADR system.

A. History of Japan's ADR

1. *"Naizai"* in the Edo Period

Except for the tradition of "Settlement before the Court" as discussed later, Japanese legal history shows a comprehensive break caused by a series of statutes adopted with the influence of foreign laws after the Meiji Restoration.

The precise details of dispute resolutions with the involvement of private third parties and not by the judicial powers during the Edo Period (1596–1868) are unknown. However, in Japanese comic story telling (*Rakugo*) and heroic story telling (*Kodan*), there are many stories of elders settling their neighborhood troubles.

O'oka justice (*O'oka Sabaki*) is the name given to rulings by Lord Tadasuke O'oka of Echizen.[20] While he was the South Magistrate of Edo, O'oka justice was a form of dispute resolution which involved the participation of the government. The public has acclaimed his decisions for years because they are flexible and free from the constraints of pre-established laws and regulations.[21] One popular story tells of a person who saw another drop three *ryo* (an old Japanese currency) and, upon seeing this, told the person that dropped the three *ryo* to take the three *ryo* for himself. The person who had dropped the money insisted that he would not take it. The two became angry and a dispute emerged between the two parties. Allegedly, in his ruling, O'oka provided one *ryo* himself and then gave each party two *ryo*. This is known as "*Sanpo Ichi Ryo Zon*" (sharing the loss among three parties each losing one *ryo*).[22] If the law were strictly applied, the result would probably be that the government would take three *ryo* as there was no one who claimed it. The following would be the value appreciated in this ruling:

1) The graceful attitude of acknowledging one's own fault by the person who dropped three *ryo*.
2) A sense of justice that one should not benefit without effort.
3) The value of clearly specifying support for both parties' way of thinking and of maintaining peace that is brought about by resuming their relationship through dispute resolution.

The stories of *Rakugo* or *Kodan* indicate that there is a long history of people favoring traditional values and flexible decisions rather than rigid rulings because flexible resolutions were applauded for promoting harmony.

Among the possible resolutions by ADR process, settlement with government involvement was frequently utilized. A judicial procedure in the Edo Period that bears close resemblance to a civil trial was called "*Deirisuji*" in contrast to "*Ginmisuji,*" which corresponds to a criminal trial. It is said that generally in "*Deirisuji,*" "*Naizai*" (private settlement in which concrete agreement was reached by mutual concession) was encouraged as a basic method for dispute resolution rather than "*Saikyo*" (an authoritative and legal judgment). This was supported by the thinking that trials for private disputes were not people's rights but rather were provided at the government's mercy.

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[20] During the Edo Period (specifically around 1677-1752), he served as magistrate for 34 years, namely as town magistrate for 19 years and a magistrate of temples and shrines for 15 years.

[21] According to HIDEMASA MAKI & AKIHISA FUJIWARA, Nihon Hōseishi (日本法制史) [HISTORY OF JAPANESE LAW] 235 (1993), "most of tales of wise judges, such as O'oka's historical episodes, are fictional and spread of those stories should be rather considered as reflection of people's thirst for heroic judges against the rigid judicial system."

[22] This is a well-known traditional comic story from the 19th century told by "rakugoka" (storytellers), such as Sanshotei Muraku.

The mediation process for "*Naizai*" was called "*Atsukai*" and the mediator was called "*Atsukai-nin.*" *Kujiyado*[23] (inns for litigation) as well as relatives, town and village officials, temples, and shrines actively worked as "*Atsukai-nin*" and were engaged in negotiation at, among others, "*Kakeai-Chaya*" (teahouses for negotiation). A private settlement agreement, when submitted to magistrate's office and approved, was given the same effect as "*Saikyo,*" a judgment by "*Deirisuji.*" Judicial officials always tried to reach "*Naizai*" during the trial.[24] The feudal government encouraged "*Naizai*" and tried to resolve disputes through settlement as much as possible, sometimes even using intimidation or physical harm. The tradition of "*Naizai*" has been passed down as "*Kankai,*" used by courts in the Meiji Period, and further as today's "Conciliation."[25]

2. *"Kankai"* in the Meiji Period

Court settlements during the Meiji Period (1868-1912) were known as "*Kankai.*" During this period, it appears that court settlement was strongly encouraged and recommending settlement was an important task for judges, and thus the number of "*Kankai*" was extremely high.[26]

Since 1875 (the 8th year in the Meiji Period), pronouncements on *Kankai* have been made many times. Among such pronouncements, the standards for judgment were articulated in Article 5 of Official Document No. 23 of Judicial Department of June 24, 1884 (the 17th year in the Meiji Period). The Article stipulated that "in conducting '*Kankai*', particular attention should be paid to understand the litigants' actual conditions and to persuade both parties to reach mutual concession." We find similar principles in this provision to those in the Civil Conciliation Act as presently in effect and in Article 3 of the ADR Promotion Act.[27] Article 1 of the Civil Conciliation Act stipulates that its purpose is to find reasonable solutions "properly corresponding to the actual conditions" by "both parties' mutual concession."[28] Article 3 of the ADR Promotion Act stipulates that "the basic principle of the ADR procedures should be to conduct the procedure fairly, while respecting the parties'

[23] "Litigations were in general conducted by litigant parties themselves. Representing litigants as a procedural agent ("*Dai-Nin*") was permitted only to their relatives or servants, etc. Masters or employees of "*Kujiyado*"(hotel for public procedures) were allowed to attend court as "*Sashizoe-Nin*"(agent) to assist in litigation proceedings, such as writing documents on behalf of the litigant or teaching the litigant techniques of litigation, and played a role of quasi professional attorney to some extent." MAKI & FUJIWARA, *supra* note 21, at 242.

[24] For a description of this process, refer to MAKI & FUJIWARA, *supra* note 21, at 233-244.

[25] *See* AKIRA ISHIKAWA & TAICHI KAJIMURA, Chūkai Minji Chōteihō (注解民事調停法) [CIVIL CONCILIATION ACT] 7 (1993).

[26] *See id.* at 7-9.

[27] ADR Promotion Act, *supra* note 8, art. 1.

[28] Civil Conciliation Act, *supra* note 1, art. 1.

voluntary efforts for dispute resolution, and aiming at finding prompt dispute resolution in such manner as properly corresponding to the actual conditions of the disputes."[29]

3. "Conciliation" in and after the Taisho Period

The Court Organization Act, which prescribed the constitution of courts of justice under the Meiji Constitution, was promulgated and came into force in 1890 (the 23rd year in the Meiji Period). In the same year, the old Civil Procedure Law was promulgated (and came into force in 1891). It abolished the system of "*Kankai*," established a system of "Settlement before the Court," and "Settlement before Trial." It also introduced a new system of arbitration. However, these settlement systems were not used as much as "*Kankai*" of the past, nor was the arbitration system used much.[30]

The recession after the World War I caused an increase in civil disputes. As a result, a series of conciliation laws were enacted, beginning with the Land Lease and House Lease Conciliation Act in 1922. Other laws that followed included the Farm Tenancy Conciliation Act (1924), the Commercial Conciliation Act and Labor Conflict Conciliation Act (1926), the Temporary Act on Conciliation of Monetary Liabilities (1932), the Personal Affairs Conciliation Act and Regulations on Compensation for Mine Pollution in the Mining Act (1939). After the start of the World War II, the Wartime Special Civil Act (1942) was enacted in order to provide for prompt resolution of civil disputes. After the war, these conciliation laws were consolidated, with reforms and adjustments, into the Labor Relations Adjustment Act (1946), the Personal Affairs Conciliation Act (1947) and the Civil Conciliation Act (1951). Thereafter, conciliations were widely used in accordance with, among others, the Civil Conciliation Act, the Family Matters Inquiries Act, the Labor Relations Adjustment Act, the Labor Union Act, and Act on Promoting the Resolution of Individual Labor-Related Disputes (enacted in 2001), and the Labor Tribunal Act (enacted in 2004).[31] Conciliations with the involvement of courts continued to be actively used.[32] In contrast, ADR by private third

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[29] ADR Promotion Act, *supra* note 8, art. 3.

[30] *See* ISHIKAWA & KAJIMURA, supra *note* 26, at 10.

[31] In addition to these laws, the Automobile Damage Compensation Security Act and the Housing Quality Assurance Act provided for conciliation by designated dispute resolution organs. These conciliations are often classified based on the third party involved in the dispute resolution, namely "Judicial ADR" in which courts are involved with the dispute but provide non-judicial resolution and "Administrative ADR" with which administrative agencies are involved as a third party.

[32] Of these conciliations, those under the Civil Conciliation Act, the Labor Tribunal Act, the Family Case Procedure Act (for family cases filed after January 1st, 2013), and the Family Matters Inquiries Act (for family cases filed before January 1st, 2013) continue to be actively used. *See* Civil Conciliation Act, *supra* note 1; Rōdō shinpanhō (労働審判法) [Labor Tribunal Act], Act No. 45 of 2004, *available at* http://law.e-

parties has not been actively used, except in limited specific areas such as traffic accidents.

4. Establishment of the ADR Promotion Act of 2004 and thereafter

In 2004, the ADR Promotion Act was enacted as a result of the recognition of the growing importance of alternative dispute resolution. The "alternative dispute resolution procedures" which are subject to the ADR Promotion Act are procedures seeking resolution of civil disputes with the involvement of third parties without applying litigation procedures. They consist of ADR with the involvement of courts such as "Settlement before the Court" and "Conciliation" as well as ADR without the involvement of courts (arbitration, mediation, and conciliation of settlement). The ADR Promotion Act sets forth the basic principles for all such ADR in general, prescribes for cooperation and coordination among those handling ADR, and defines the responsibilities of national and local governments for promoting ADR.[33] In addition, the ADR Promotion Act established, with a view towards encouraging mediation in the private sector without the involvement of courts, a system where the Ministry of Justice may issue certificates to private ADR institutions.[34] Despite the purpose of the ADR Promotion Act being to promote ADR without the involvement of courts, such ADR, including international ADR in Japan, generally remains inactive. Their number is extremely small compared to the number of cases resolved by judicial decisions of courts or cases by involvement of courts, namely "Settlement before the Court" or "Conciliation." The number of cases brought to ADR institutions such as the Japan Shipping Exchange, the Japan Commercial Arbitration Association, or the Dispute Resolution Centers of Bar Associations is not large.

The number of ADR cases that do not involve courts in Japan is extremely small in comparison with foreign countries. While the rest of the world experienced rapid development of international arbitration or mediation since the 1990's, Japan has not. However, if ADR involving courts are combined with those not involving courts, the total number of ADR cases in Japan would not be so different from other countries.

B. The Standards of Judgment for Domestic ADR under Existing Japanese Laws

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gov.go.jp/announce/H16HO045.html; Kaji jiken tetsuzukihō (家事事件手続法) [Family Case Procedure Act], Act No. 52 of 2011, *available at* http://law.e-gov.go.jp/announce/H23HO052.html.

[33] ADR Promotion Act, *supra* note 8, art. 4.

[34] *Id.* art. 5.

Insofar as the procedures and standards for judgment with respect to conciliation or settlement with the involvement of courts are concerned, it seems that the requirement of "Rule of Law" has presumably been satisfied due to the involvement of courts. This would be the main reason why the standards of judgment for ADR with the involvement of courts have not been squarely raised as a significant issue. However, for example, in a case where a judge is to rule in a court case after having spoken with the parties separately during a failed settlement procedure involving the same court, the procedure taken might be against notions of due process. This kind of issue has not been adequately addressed.

Most ADR in Japan involves the courts. Therefore, arguments on the standards of judgment for domestic ADR have focused on the interpretation of statutes concerning Conciliation. It seems that the standards of judgment for ADR without the involvement of courts have not been discussed extensively. Here, I would like to review all laws and regulations of Japan currently in effect concerning the standards of judgment for ADR in Japan.

1. The ADR Promotion Act[35]

Article 1 (ADR procedures)

Article 1 of the ADR Promotion Act defines alternative dispute resolution as "procedures of resolution for a civil dispute between parties who seek, with the involvement of a neutral third party, a resolution without using litigation procedure." No restriction is set on the "third party" that can be involved in the alternative dispute resolution process, except for the requirement that it shall be "neutral." Third parties may include national or local governments that conduct administrative ADR, courts that conduct so-called judicial ADR, including conciliation with the involvement of courts, and private ADR institutions or those individuals who conduct *ad hoc* ADR. Therefore, it includes both civil ADR, such as arbitration or mediation of settlement, and court-involved ADR, such as conciliation. With respect to private ADR institutions, the ADR Promotion Act provides a certification system for them in connection with their mediation of settlement.[36] The financial ADR system is a system aiming at dispute resolution by private ADR institutions through "mediation of settlement" as defined in the Act.

Article 3-1 (Basic principle of ADR procedures)

Article 3-1 of the ADR Promotion Act sets forth the basic principle for alternative dispute resolution procedures and reads "Alternative dispute resolution procedures shall, as one of the procedures for settling disputes by law, be executed in a fair and appropriate manner while respecting the

[35] *Id.*

[36] *Id.* art. 5.

disputing parties' voluntary efforts for dispute resolution, and be aimed at finding prompt dispute resolution based on specialized expertise and in such manner as properly corresponding to the actual conditions of the dispute." This principle is applied to all "alternative dispute resolution procedures" defined in Article 1.

Article 6 (Certification standards by the Minister of Justice)

Article 6 of the ADR Promotion Act sets forth various requirements which a provider of dispute resolution services must comply with before receiving certification from the Minister of Justice with respect to their conduct of alternative dispute resolution. For example, Item 5 of Article 6 of the ADR Promotion Act requires that when the person who is conducting the alternative dispute resolution process is not a lawyer, a qualified attorney must be available for consultation on the interpretation of any laws or regulations that require specialized knowledge.

Supplementary Resolutions on the ADR Promotion Act

According to Paragraph 3 of the Supplementary Resolutions of the Judicial Affairs Committee of the House of Representatives made at the stage of deliberating on the ADR Promotion bill, "concerning the rules of alternative dispute resolution procedures from the beginning to the end by private bodies, the principles to be applied in case of disagreement of the parties, and legislation of such principles if necessary, shall be examined giving due regard to the international movement and trend in respect of the subject." Similarly Paragraph 6 of the Supplementary Resolutions of the Judicial Affairs Committee of the House of Councilors states, "concerning the rules of conciliation or mediation or other ADR procedures from the beginning to the end by private parties, legislation of the principles to be applied in case of disagreement among the disputing parties shall be continuously examined giving regard to the variation of private dispute resolution procedures and to the future international movement and trend in respect of the subject." Also, Paragraph 4 of the Supplementary Resolutions of the Judicial Affairs Committee of the House of Councilors states, "concerning the measures to ensure an attorney is available for consultation when specialized expertise on the interpretation and application of laws and regulations is required in the process of providing private dispute resolution in cases where the dispute resolution provider is not qualified as an attorney, it is required to ensure fair and appropriate procedures and to ensure careful attention so as not to harm the interests of alternative dispute resolution participants." These supplementary resolutions of the ADR Promotion Act show that the legislators wished to continue to examine the necessity of legislation or other measures to ensure fair and appropriate standards for procedures. From these Resolutions we could understand that the legislators' intention was to continue to watch the progress and development of the ADR practice.

2. The Civil Conciliation Act[37]

While Civil Conciliation is a court-involved dispute resolution procedure for civil affairs, it is also an "alternative" dispute resolution procedure in that it is a dispute resolution procedure without the use of litigation procedures. It aims at dispute resolution by agreement of the concerned parties. In Japan, conciliation has been practiced for many years and a large body of precedents has accumulated during this time. Conciliation in Japan has a longer history than "court-annexed ADR" in the US or the UK.[38] Among the various alternative dispute resolution methods, the standards for judgment in Civil Conciliation procedures have been the most extensively examined and discussed in Japan.

Article 1 (Judgment standards)

Article 1 of the Civil Conciliation Act clarifies the purpose and nature of the conciliation system. It states that the Civil Conciliation "aims at finding such a resolution of disputes of civil affairs, by mutual concession of the disputing parties, as is fair and reasonable and is suitable in properly responding to the actual conditions of the case." This language shows the standards for judgment for ADR aimed at dispute resolution by settlement between disputing parties without resorting to litigation procedures. As such the standards for judgment as expressed by this language shall be appropriate as the standards for similar ADR procedures without the involvement of the court, but with the involvement of private third parties.

Article 1 of the Civil Conciliation Act states that the principle procedure shall be "mutual concession of the disputing parties" and the standards of judgment for dispute resolution is "fair and reasonable and suitable in properly responding to the actual conditions of the case." Because dispute resolution is made by an agreement between the parties, the agreement between the parties must be "fair and reasonable and suitable in corresponding to the actual conditions of the case." The standard for judgment to be used by the judge who presides over the Civil Conciliation procedure is simply "fair and reasonable (*Jori*)." From this fact, we must question any possible differences between the standards for judgment in Civil Conciliation and the substantive Japanese law. At least it will be interpreted that the "fair and reasonable (*Jori*)" test does make the decisions of conciliation, insofar as satisfying this test,

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[37] Civil Conciliation Act, *supra* note 1.

[38] The US courts started using ADR in the mid-1970s. The Civil Justice Reform Act of 1990 permitted the federal courts to use ADR. Afterwards, courts in the UK, Canada, and Australia started using ADR. However, in contrast to judges in continental law countries, judges in the US and the UK are not involved with the content of settlements, but rather stay the judicial procedure in order to have the parties attempt to resolve their disputes by following ADR procedures. At any rate, the court's use of ADR originated from the awareness that court proceedings alone do not provide sufficient access to civil justice due to problems of expense and efficiency. *See* HENRY BROWN & ARTHUR MARRIOTT, ADR PRINCIPLES AND PRACTICE 84–102 (1993).

legitimate in supplementing any possible lack of the substantive Japanese law. It should be noted that Civil Conciliation has a role in forming (creating) right by being a forum for generating and approving a new right as such.[39]

Article 14 (Failure of Conciliation)

Article 14 stipulates that "if the conciliation committee[40] considers the agreement between the parties is not appropriate it may end the case by declaring a failure of conciliation," unless a court renders a decision as stipulated by Article 17. Even in cases where an agreement is reached between the parties, the establishment of conciliation is not approved if the content of such agreement is illegal or otherwise materially inappropriate in light of the "fair and reasonable (*Jori*)" test. The need for the conciliation committee's approval of the validity of the content of an agreement shows that Civil Conciliation is a judicial dispute resolution system before the court to contribute to the public interest for realizing justice and equity. This will lead to an interpretation that the standards of judgment required by Article 14 are "justice and equity," but those requirements could also be interpreted into the "fair and reasonable (*Jori*)" in Article 1.

Article 17 (Decision in lieu of Conciliation)

Article 17 provides courts with the authority to make a decision in lieu of conciliation. In case there is no possibility for reaching conciliation by the conciliation committee the court "may, by exercising its authority at its own initiative, make a decision necessary to resolve the case to the extent that it does not go beyond allegations of the both parties," after "hearing from the civil conciliation members of the relevant conciliation committee, taking the equity of both parties into consideration and looking at all the circumstances."

"Taking the equity of both parties into consideration" is similar to the requirement of being "fair and reasonable," as stipulated in Article 1; "looking at all the circumstances" is similar to finding "a resolution in such manner as properly corresponding to the actual conditions," as stipulated in Article 1. Thus, it is the "fair and reasonable (*Jori*)" test itself rather than the law as it is that forms the basis for the decision making.[41] In short, the criterion which courts should depend on in making a decision in lieu of conciliation (the decision criterion) is not different from the criterion on which the conciliation organs depend on in conciliation (the conciliation criterion). It is nothing but the "fair and reasonable (*Jori*)" test as stipulated in Article 1.

There is a view that a resolution of dispute which satisfies the "fair and reasonable (*Jori*)" test falls under one of the three cases.[42]

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[39] *See* ISHIKAWA & KAJIMURA, *supra* note 25, at 51-55.

[40] The conciliation committee shall consist of one conciliation chief, who shall be designated from among judges, and no less than two civil conciliation members.

[41] *See* ISHIKAWA & KAJIMURA, *supra* note 25, at 244.

[42] *See id.* at 249-250.

The first is a resolution which is consistent with statutes, such as civil and commercial law, or other substantive laws, including laws emerging from customs or court judgments.

The second is a resolution which is made free from a result of the application of law (other than mandatory law). In circumstances where it is impossible to reach a proper resolution by application of law (other than mandatory law), a resolution can be made by seeking a proper resolution corresponding to the actual conditions of the case rather than applying the law (other than mandatory law) to the case. In these situations, we can see creation of law.

The third is a resolution which is made directly by application of the "fair and reasonable (*Jori*)" test in such circumstances where there is no applicable substantive law. Such resolution is made in cases where we cannot reach a proper resolution by interpretation of statutes or other sources of law nor by applying general rules of law such as the principle of faithfulness and sincerity (*Shingisoku*) or the disallowance of abuse of right (*Kenriranyou*).

In further discussing the release from the application of law (other than mandatory law) as set forth in the second case, we could say that even if a resolution does not accord to the result of applying the given laws, it can be a resolution which satisfies the "fair and reasonable (*Jori*)" test. In other words, it is a resolution resulting from the application of law (other than mandatory law) in such a way as has been considered reasonable and the interpretation of relevant law is not required to be consistent with court precedents.

The "fair and reasonable (*Jori*)" test could reflect, when functioning as the conciliation criterion or the decision criterion, the common sense prevailing in society. In other words, it means what society considers "fair and reasonable" in light of the people's common sense.

3. The Standards of Judgment for Arbitral Awards under the Arbitration Act[43]

Article 36, Paragraph 1 (Standards for arbitral awards)

Article 36, Paragraph 1 of the Arbitration Act provides that the "the governing law in accordance with which arbitral tribunal shall render arbitral awards shall be the one agreed upon by the parties." Paragraph 2 of Article 36 provides to the effect that in the absence of agreement between the parties, the arbitral tribunal shall apply the laws of the State which is most closely connected with the case. Paragraph 3 of the said Act then provides that "notwithstanding the provisions prescribed in the preceding two paragraphs, the arbitral tribunal shall decide according to the principle of fairness and good (*ex aequo et bono*) if expressly requested by the parties to do so." Further, Paragraph 4 provides that "where there is a contract, the arbitral tribunal shall decide in accordance with the terms of such contract, and if there is custom

[43] Arbitration Act, *supra* note 2.

applicable to the relevant civil dispute, the arbitral tribunal shall take into account such custom."

According to Paragraph 1 through Paragraph 3 above, arbitral awards must be rendered by application of law. From the intent of Article 45, Paragraph 2 as described below, arbitrators can apply the law (other than mandatory provisions of law) in such manner as they may consider appropriate in light of the circumstances of the case. According to the Act the arbitral tribunal shall decide according to the "principle of fairness and good (*ex aequo et bono*)" and can depart from the result of application of law, only if the parties have expressly requested to do so, but no guidance is given in the Act as to what exactly constitutes or means the "principle of fairness and good (*ex aequo et bono*)."

Article 45, Paragraph 2 (Grounds for refusing to recognize an arbitral award)

Under Article 45, Paragraph 1 of the Arbitration Act, an arbitral award has the same effect as a final and conclusive court judgment except in the cases set forth in Article 45, Paragraph 2 of the Arbitration Act. Therefore, it is understood that, except for the cases set forth in Article 45, Paragraph 2 of the Arbitration Act, current Japanese law treats an award in arbitration the same as a court decision and recognizes it as an appropriate resolution to a dispute in the Japanese judicial system.

The grounds for refusing to recognize an arbitral award listed in Article 45, Paragraph 2 of the Arbitration Act are as follows:

i. the arbitration agreement is not valid (Items (1) and (2));
ii. a party was not given proper notice of the appointment of an arbitrator or of the arbitration proceedings, as required by the law of the jurisdiction in which the site of arbitration is located (Item (3));
iii. a party was otherwise unable to present its case in the arbitral proceedings (Item (4));
iv. the arbitral award contains decisions on matters beyond the scope of the submission to arbitration or the claims which gave rise to the arbitral proceedings (Item (5));
v. the composition of the arbitral tribunal or the arbitral proceedings was not in accordance with the law of the jurisdiction in which the site of arbitration is located (Item (6));
vi. the arbitral award has not yet become binding on the parties under the law of the jurisdiction in which the site of arbitration is located, or the arbitral award has been set aside or suspended by a court of such jurisdiction (Item (7));

vii. the subject matter of the dispute is not capable of settlement by arbitration under the laws of Japan (Item (8)); or

viii. the content of the arbitral award would be contrary to the public policy or good morals of Japan (Item (9)).

The grounds for suspending arbitral awards are substantially the same as the aforementioned grounds, except that they do not include the ground described in (vi) above (Article 44, Paragraph 1).

The grounds set forth in items (ii), (iii), (v) and (vi) above are related to matters of "due process" and those set forth in items (i), (iv), (vii) and (viii) above are related to matters of the content of arbitral awards. Of these, only item (viii) deals with standards of judgment for resolution of a dispute by arbitration.

The provisions prohibit courts from refusing to recognize arbitral awards or from suspending them except in cases where such arbitral awards are contrary to public policy or the good morals of Japan. It requires that courts should not examine an arbitrator's application of law except as it relates to public policy. In other words, courts accept that arbitrators can interpret and apply the law at their discretion, except where it relates to the public policy and good morals. Courts may refuse to recognize an arbitral award or suspend such award only when the arbitral award is contrary to public policy or good morals. In general this means that courts may do so only when the arbitral award is in breach of mandatory provisions of law.[44]

C. Standards of Judgment for Foreign ADR Awards Recognized under Japanese Law

Arbitral awards made in foreign countries are recognized under Japanese law in accordance with the framework for recognition of arbitral awards set forth in the Arbitration Act.45 Can standards of judgment for foreign arbitral

[44] In the US, there is a judicial decision that held "manifest disregard of the law" is a ground to refuse recognition in addition to those grounds to refuse recognition provided in the Federal Arbitration Act. *Wien & Malkin LLP v. Helmsley-Spear, Inc.*, 783 N.Y.S.2d 339 (N.Y. App. Div. 2004) rev'd, 846 N.E.2d 1201 (N.Y. 2006) (reversed by the court of appeals on the grounds that the arbitration panel did not manifestly disregard the law). Professor Hans Smit of the Columbia Law School stated that "manifest disregard of the law" is a ground for non-recognition of an arbitral award only when the law disregarded is of a mandatory nature and, in either application of law or fact-findings based on evidence, arbitrators may decide freely based on what they consider reasonable without being bound by court's interpretation of non-mandatory law. This is a matter-of-course to result from seeking flexible resolution of disputes by arbitrators. *See* Hans Smit, *Manifest Disregard of the Law in the New York Court of Appeals*, 15 THE AM. REV. OF INT'L ARB. 315, 315–19 (2005). This interpretation is similar to the interpretation of Article 45, Paragraph 2 of the Arbitration Act of Japan, as discussed above in Section 3.

[45] Arbitration Act, *supra* note 2, art. 45.

awards to be recognized under Japanese law be considered a part of the standards for ADR under Japanese law? As far as the "standards of judgment" here means, standards for foreign arbitral awards should not be regarded as a part of the "standards" for ADR under Japanese law, but are only reflected in such standards for ADR under Japanese law indirectly as a result of applying the framework of recognition of foreign arbitral awards.

Mediation or other forms of ADR (other than arbitration) conducted in foreign countries have no legal effect under Japanese law except that Japanese law may give effect to contracts for settlement agreements reached in the relevant ADR procedures. The question of whether Japanese law recognizes standards of judgment applied in such ADR has not been raised. Therefore, unlike the arbitral awards, there is no reason to understand that the standards of judgment for such foreign ADR procedures are incorporated into Japanese law in any respect.

1. Recognition of Foreign Arbitral Awards

Irrespective of whether or not the arbitration took place in Japan, according to Article 45, Paragraph 1 of the Arbitration Act, an arbitral award shall have the same effect as a final and conclusive judgment except in those cases listed in Article 45, Paragraph 2 of the Arbitration Act. Therefore, it is understood that irrespective of whether or not the site of arbitration is in Japan, and except for cases listed in Article 45, Paragraph 2 of the Arbitration Act, current Japanese law recognizes decisions made in arbitrations as having been made in accordance with law, and recognizes them as an appropriate dispute resolution under the Japanese judicial system. If the site of arbitration is in Japan, the standards for such decisions shall be as prescribed in Article 36 of the Arbitration Act. However, with respect to the standards of judgment for arbitral awards of an arbitration whose site is located in a foreign jurisdiction (hereafter, "foreign arbitral awards"), Japanese law defers to the laws of the relevant foreign jurisdiction subject to Article 45, Paragraph 2 of the Arbitration Act.

The grounds for refusing recognition of foreign arbitral awards is the same as the grounds for refusing recognition of domestic arbitral awards as described above in Article 45, Paragraph 2. Among the grounds of refusal listed items (ii), (iii), (v), and (vi) relate to "due process" and items (i), (iv), (vii) and (viii) relate to the content of the arbitral award. Of these, only (viii) deals with standards of judgment for resolution of a dispute that is the subject of settlement by arbitration.

The framework of recognition of foreign arbitral awards leads us to conclude that, except for the cases listed in Article 45, Paragraph 2 of the Arbitration Act, Japanese law recognizes, without questioning the standards for judgment with respect to procedural or substantive issues, that foreign arbitral awards satisfy the requirements under Japanese law for "rule of law" and "due process" for protection of rights. This is consistent with the principle of private international law of Japan and with the principle of recognition of foreign court judgments that the foreign law determined by applying the

private international law of Japan and foreign court judgments shall be applied or recognized generally regardless of the content of such foreign law or judgments, except when the result of such application or recognition shall be contrary to the "public policy or good morals" of Japan.[46]

2. The Standards of Judgment in International Arbitration

What are the standards for judgment in foreign arbitral awards, which current Japanese law accords the same effect as the final and conclusive court judgment as stated above?

International arbitration has developed rapidly since the 1990's. Cross-border business activities have increased and areas of trade and investment expanded from developed countries to developing countries. Parties of different jurisdictions to a cross-border dispute would sometimes feel uneasy to leave resolution of such dispute in the hands of the court of the other party's jurisdiction. By virtue of the recognition and enforcement system under the New York Convention, international arbitration has provided a dispute resolution system that replaced the dispute resolution by national courts of any particular jurisdiction.[47]

The locations most often selected by the parties for international arbitration are, among others, Paris, London, Geneva, Stockholm, New York, Singapore and Hong Kong.

While an international arbitration whose site is located in a foreign country is subject to supervision of that country's courts in accordance with its laws, the arbitration proceedings are in many cases conducted in accordance with the rules of the arbitration institution selected by the parties such as the ICC, LCIA, or AAA. The soft law comprising the rules of such institutions as well as the guidelines of the IBA, which is not national law of any jurisdiction, increasingly plays an important role in determining how arbitral proceedings are conducted.[48]

The challenge for international arbitration is to make a fair final decision in the context of the two conflicting demands, namely the pursuit of efficiency

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[46] *See* Hō no tekiyō ni kansuru tsūsokuhō (法の適用に関する通則法) [Act on General Standards for Application of Laws] Act No. 10 of 1898, art. 45 (amended 2006), *available at* http://law.e-gov.go.jp/announce/H18HO078.html; Minji soshōhō (民事訴訟法) [Code on Civil Procedure] Act No.109 of 1996, art. 118 (amended 2012), *available at* http://law.e-gov.go.jp/htmldata/H08/H08HO109.html.

[47] The eminent former British judge and arbitration expert Lord Mustill said that the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (the New York Convention) "perhaps could lay claim to be the most effective instance of international legislation in the entire history of commercial law." Lord Mustill, *Arbitration: History and Background*, 6 J. INT'L ARB. 43 (1989).

[48] For further discussion on soft laws in international arbitration, see William Park, *The Procedural Soft Law of International Arbitration*, *in* PERVASIVE PROBLEMS IN INTERNATIONAL ARBITRATION (Loukas A. Mistelis ed., 2006).

in dispute resolution (the pursuit of prompt and easy dispute resolution) on the one hand and the compliance with due process on the other. Experts involved in international arbitration, including arbitration institutions and associations of lawyers, are called on to examine a number of issues such as the procedures for collecting evidence which differ between common law countries and civil law countries, and they make proposals on those issues. Their efforts aim at reaching an agreement to resolve difficult challenges and establishing a better practice in international arbitration.

Currently, international arbitration is not only widely used as a dispute resolution procedure among private parties, but is also used as a dispute resolution mechanism for numerous number of investor and State disputes. The disputes are between a State and investor of another State under an international treaty between the two States, such as bilateral investment treaty or economic partnership agreement, which has been entered into for the purpose of protecting investment in these States and in which each State has committed itself to international arbitration in respect of such disputes. As a result, international arbitration deals with more than just private rights. It also involves public policy, leading to skepticisms about confidentiality which has been traditionally recognized as an advantage of international arbitration. As will be discussed herein, the financial ADR systems that have been established in many countries and have developed to form an international network to exchange their respective experiences are another form of ADR involving public policy.

In those countries in which the principles of modern law, such as "the rule of law" or "due process" for protection of rights prevail, just as in Japan, consistent efforts have been made to ensure that the dispute resolution by means of international arbitration will qualify as a "dispute resolution by law." Apart from the standards of judgment chosen by agreement between the parties, the standards for judgment in international arbitration will, due to their diversity and flexibility, necessarily be described by an abstract principle. If I would venture to say, it would be a "fair and reasonable" judgment. It could be restated in different ways corresponding to specific circumstances in the proceedings and nature of the dispute.

D. Standards of Judgment for ADR under the Rule of Law

1. The Meaning of the "Rule of Law" and its Change in Modern Society

The Constitution of Japan adopted during the Meiji period was guided by the concept of the "constitutional state" of the German jurisprudence. In contrast, it is believed that the present Japanese Constitution adopted the principle of "the rule of law" which originated from Anglo-American law tradition, although there are different opinions about this.[49] The idea of "the

[49] One view, argued by Professor Yoshimoto Yanase, is that it does not adopt the rule of law, at least in terms of the meaning described by Dicey. Nobunari Ukai, Hō no shihai

rule of law" can be found in Article 31 (right to due process), Article 29 (property right), Article 14-1, (equality under the law), Article 32 (right of access to the courts), Article 37 (various rights of criminal defendant), Article 76-2 (prohibition of extraordinary tribunals) of the Constitution of Japan. However, the Constitution of Japan includes provisions indicating a shift in the meaning of the principle of "the rule of law," as will be described below. Those include Article 25, stipulating people's right to maintain the minimum standards of wholesome and cultural living and the State's obligation to use its endeavors for the promotion and extension of social welfare and security and public health.

According to Albert Dicey,[50] the "rule of law" means first, "due process of law" and second, "the principle of administration governed by laws and judicial state." The first principle requires a proper notice of hearing and otherwise provides an opportunity to the defendant to represent the case and requires the plaintiff to fulfill the responsibility of proving the facts of violation of rights in accordance with strict rules of evidence. The second principle requires the administration governed by laws and if the government violates laws, judgment on violation shall be made, and relief shall be given, exclusively by judicial power rather than by administrative power.[51]

Individual's freedoms and rights are secured by the theory that both State and individuals shall become acknowledged as legal person qualified to enjoy rights and to assume obligations, and to do such acts as will produce any legal effect, only to the extent as prescribed and in accordance with law. The original meaning of "the rule of law" as such is unchanged. In modern society, however, it has come to be recognized that the "relief" of individuals is necessary in the economic system which had been established based on freedom and equality. Under such circumstances, there has been a growing demand in the society that administrative power should exercise its influence on the society. It has been acknowledged that the procedures for dispute resolution in modern society do not necessarily have to be the same as judicial trials but the society requires such procedures to be capable of finding efficient and fair resolution with the most appropriate knowledge. Thus, it is recognized that there are such areas that will require administrative decisions which cannot be considered as judicial, and the private ADR system capable of finding prompt resolution corresponding to the actual circumstances of dispute, by virtue of effective use of experts, is becoming increasingly important.

2. The Rule of Law in ADR

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no gendaiteki igi (法の支配の現代的意義) [*Modern Significance of the Rule of Law*], 32 Hō no shihai (法の支配) [RULE OF LAW] 3, 7 (1977).

[50] Albert Venn Dicey (1835-1922), a British jurist.

[51] *See* Ukai, *supra* note 49, at 10–12.

It is understood that the protection of individual rights in the United Kingdom under the principle of the "rule of law" was not secured by codification of such rights in written statutes, but was established rather by the general principle of law concerning human rights which resulted from court decisions protecting individual human rights in individual cases. The law in this context includes not only statutory law but also natural law and customary law and they come to be recognized and clarified as existing law through accumulation of court decisions.[52] This course of development and establishment of "the rule of law" in the UK encourages us to explore the standards of ADR in the UK and provides those engaged in ADR process with important guidance for making their decisions.

What is required in ADR judgment by "the rule of law" and the "due process" for protection of rights under the present Japanese law? With respect to arbitration, considering not only the standards for domestic arbitration provided in Article 36 of the Arbitration Act but also the requirements for recognition of arbitral awards, including foreign arbitral awards, provided in Article 45 of the same Act, we can understand that arbitral awards satisfy these requirements with respect to both proceedings and judgment on merits if none of the grounds to refuse recognition of arbitral awards as provided in the Article 45, Paragraph 2 of the Arbitration Act are present. The Act shows only a negative list and does not provide for any guideline to observe in making judgments.

The framework is the same as the one that many countries adopt for arbitration. The Arbitration Act of Japan was enacted following, with only slight modifications, the UNCITRAL Model Law on International Commercial Arbitration adopted by the United Nations Commission on International Trade Law, UNCITRAL, in 1985. The framework for recognition of foreign arbitral awards set forth in Article 45 of the Arbitration Act as well as the grounds for refusing recognition of arbitration awards as listed in Paragraph 2 of the same Article, are based upon Article 35 and Article 36 of the UNCITRAL Model Law in compliance with Article V of the "Convention on the Recognition and Enforcement of Foreign Arbitral Awards" (New York Convention). The New York Convention was made in 1958 and currently 146 states are members of the Convention. As a result, the framework for recognition in foreign countries of arbitral awards is acknowledged and in force widely in the international community, while in contrast no similar international framework exists in respect of the recognition of court decisions.

The framework under Japanese law for the recognition of foreign arbitral awards entrusts, as in the case of the laws of many other countries, detailed standards for judgment in foreign arbitration to foreign laws and regulations. Japanese law does not explicitly define the standards for making decisions in foreign arbitration. This indicates that Japanese law allows a wide discretion in respect of the standards of judgment in dispute resolution by ADR, but it

[52] *See id.* at 9. Human rights in the United Kingdom are now also covered by the European Convention for the Protection of Human Rights and Fundamental Freedoms.

requires, by Article 45 of the Arbitration Act,[53] that such judgment should be made under the supervision of the relevant foreign court and be within the discretion which the laws of the same foreign country permit. Japanese law admits that "the rule of law" is satisfied through foreign laws, but does not allow arbitrators to exercise their discretion, in respect of the standards of judgment under Japanese law for arbitration, beyond this framework of Japanese law.

The framework under Japanese law for the recognition of foreign arbitral awards, as described above, results in practically providing arbitrators with very broad freedom with respect to standards of judgment in dispute resolution by arbitration. Should such a broad freedom be granted only to arbitrators? Such a broad freedom is permitted under the modern principle of "rule of law," and we do not see any reason why the same principle should permit such broad freedom for arbitration but not for other forms of ADR.

ADR, which pursues dispute resolution out of courts, tends to go beyond borders which establish the territorial limit of national sovereignty. In addition, those disputes which are submitted to ADR are often common in nature in the international community. Accordingly it is reasonable to foresee that ADR in Japan is affected by ADR practice in foreign countries. With this perspective, several issues can be identified with respect to ADR in Japan. How should the principles common to all democracies, such as the "rule of law" or "due process" be satisfied in ADR procedures in Japan? What should be the proper meaning of each of the principles of alternative dispute resolution in the ADR Promotion Act of Japan, such as "fair," "appropriate," and "prompt resolution properly corresponding to the actual conditions of the dispute," or the "fair and reasonable (*Jori*)" test that the Civil Conciliation Act provides as the norm of conciliation and the norm of decision? What should be the proper interpretation of the "laws directly applied to the facts," or the "equity and good faith," which the Arbitration Act of Japan adopts as standards of judgment in arbitration? The ADR in foreign countries must have similar issues. Such being the circumstances, the standards for judgment in dispute resolution by ADR in foreign countries should affect the standards for ADR in Japan. Both standards would develop in the same direction in response to the needs for ADR.

IV. THE STANDARDS OF JUDGMENT FOR FINANCIAL ADR IN THE UK

In the following sections I will review the standards for judgment in dispute resolution of the ombudsman of Financial Ombudsman Service Limited of the UK (hereafter referred as "UK FOS" or simply "FOS") which was established in accordance with the Financial Services and Markets Act 2000

[53] Arbitration Act, *supra* note 2, art. 45.

(hereafter referred as "FSMA 2000").[54] In addition, I will review international cooperation among EU member states aimed at resolving cross-border financial service disputes efficiently for the benefit of customers, as well as international efforts of financial ombudsman systems of various countries to improve their services by exchanging their respective experiences.

The Financial ADR system in the UK differs from the Japanese system. However, there are a number of issues common to both systems. I would like to introduce the UK system in some detail, with a view to providing useful information for considering various issues which may arise in ADR practices in Japan.

A. The Standards of Judgment for Dispute Resolution by Ombudsman of the UK FOS

1. The History and Size of the UK FOS

Starting with the "Insurance Ombudsman" founded in 1981, a number of financial service industries established their respective schemes by which disputes with their customers are resolved out of courts with third party intervention. The FSMA 2000 integrated nine existing regulatory bodies into the Financial Services Authority (hereafter referred as "FSA") and integrated eight existing Ombudsman systems to establish the UK FOS. According to the annual review published by the UK FOS for the year ending March 31, 2012,[55] the total number of enquiries and complaints that Customer-contact Division of the UK FOS handled was 1,268,798; the number of new cases referred to adjudicators and ombudsmen was 264,375, of which 60% (157,716 cases) were about the sale of payment protection insurance ("PPI"); and 201,793 cases were resolved by adjudicators through mediation, recommended settlements and adjudications and 20,540 cases were resolved by the decision of ombudsmen. The number of disputes resolved by the UK FOS during the same year was 222,333. Apart from PPI complaints, on which a legal action was taken against FOS,[56] almost 40% of all disputes were resolved within three months and two thirds of all disputes within six months. FOS operated on a cost-base of £108 million and with 1,700 staff at the end of the year.

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[54] FINANCIAL SERVICES AND MARKETS ACT 2000 was amended by the Financial Services Act of 2010 to reform the UK financial supervision system, but the provisions relating to UK FOS have not been amended.

[55] Financial Ombudsman Service, Annual Review Financial Review 2011/2012, *available at* http://www.financial-ombudsman.org.uk/publications/ar12/ar12.pdf. Information for the financial year 2012/2013 is available on the FOS website.

[56] The legal action was bought by the British Bankers' Association on behalf of a number of banks against FSA and UK FOS, in the form of judicial review, to challenge the FSA's guidance and FOS approach to PPI cases. The court judgment rendered in April 2011 endorsed the FSA and FOS position, and in May 2011 the British Bankers' Association confirmed that they would not appeal against the judgment.

2. UK Statutory Provisions on the Standards for Judgment and on Procedures

In Part XVI of SCHEDULE 17 The Ombudsman Scheme where the Ombudsman Scheme is provided, the FSMA 2000 stipulates the purpose of the Ombudsman Scheme in Section 225 (1) as follows:[57]

> 225(1) This Part provides for a scheme under which certain disputes may be resolved quickly and with minimum formality by an independent person.

Section 228(2) stipulates on determination of the disputes which are subject to the compulsory jurisdiction of the UK FOS as follows:

> 228 (2) A complaint is to be determined by reference to what is, in the opinion of the ombudsman, fair and reasonable in light of all the circumstances of the case.

Also, Section 229(2) and (3) stipulate on awards as follows:

> 229 (2) If a complaint which has been dealt with under the scheme is determined in favor of the claimant, the determination may include:
>
> > (a) an award against the respondent of such amount as the ombudsman considers fair compensation for loss or damage (of a kind falling within subsection (3)) suffered by the claimant ("a monetary award");
> > (b) a direction that the respondent take such steps in relation to the complaint as the ombudsman considers just and appropriate (whether or not a court could order those steps to be taken).
>
> 229 (3) A money award may compensate for:
>
> > (a) financial loss; or
> > (b) any other loss, or any damage, of a specified kind.

The UK FOS's scheme rules (hereafter referred as "FOS Rules"), which were made under the authorization by SCHEDULE 17, stipulate the rules for dispute resolution as follows:[58]

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[57] FINANCIAL SERVICES AND MARKETS ACT, *supra* note 3.

[58] 25 FINANCIAL CONDUCT AUTHORITY, *Complaint Handling Procedures of the Financial Ombudsman Service*, *in* FINANCIAL CONDUCT AUTHORITY HANDBOOK, ch. 3 (2003).

> 3.8.1 R (1) The Ombudsman will determine a complaint by reference to what is, in his opinion, fair and reasonable in all the circumstances of the case.
>
> (2) In considering what is fair and reasonable in all the circumstances of the case, the Ombudsman will take into account the relevant law, regulations, regulators' rules and guidance and standards, relevant codes of practice and, where appropriate, what he considers to have been good industry practice at the relevant times.

Part III The Compulsory Jurisdiction requires in Section 14(1)[59] that the UK FOS shall make rules on procedures for filing complaints and further enumerates in Section 14(2) the items to be determined by the rules. Subsection (a) and (d) of Section 14(2) provide as follows:[60]

> (2) Scheme Rules may, among other things: ---
>
> (a) specify matters which are to be taken into account in determining whether an act or omission was fair and reasonable;
>
> (d) make provision as to the evidence which may be required or admitted, the extent to which it should be oral or written and consequences of a person's failure to produce any information or document which he has been required (under section 231 or otherwise) to produce;

3.5.1 R of the FOS Rules authorizes the Ombudsman to give directions as to the extent to which the evidence required and determines whether a complaint should be oral or written. In addition, the FOS Rule and Guidance address, as set forth blow, whether the Ombudsman should be required to hold a hearing in public or in private.[61]

> 3.2.13 R A party who wishes to request a hearing must do so in writing, setting out the issues he wishes to raise and (if appropriate) any reasons why he considers the hearing should be in private, so that the Ombudsman may consider whether

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[59] Financial Services and Markets Bill, 1999-2000, H.C. HC Bill [1] cl.15(1).

[60] *Id.* cl.15(2)(a)-(d).

[61] *See* FINANCIAL CONDUCT AUTHORITY HANDBOOK, *supra* note 58, Chapter 3.

the issues are material, whether a hearing should take place and, if so, whether it should be held in public or private.

3.2.14 G In deciding if there should be a hearing and, if so, whether it should be in public or private, the Ombudsman will have regard to the provisions of the European Convention on Human Rights.

3. Judicial Review of the Decision of the UK FOS

If a complaint petitioner is not satisfied with the Ombudsman's decision, the petitioner can bring a lawsuit with the court on the same subject but the financial service provider is bound by the Ombudsman's decision. However, since the UK FOS is a public organ, financial service providers have the rights to demand judicial review as to whether the content of Ombudsman's decision and the process of reaching the decision exceeds the scope of discretion granted to Ombudsman under the FSMA 2000 or whether it violates the principle of rule of law or infringes the constitutional rights, although there is no express provision in the FSMA 2000 to this effect.

In *R (Heather Moor & Edgecomb Limited) v Financial Ombudsman Service and Simon Lodge*,[62] the UK Court of Appeal gave, in its decision of June 11, 2008 on judicial review, a detailed opinion with respect to the UK FOS system and the standards for judgment in dispute resolution by Ombudsman and the scope of its discretion. This is the leading case on this matter.

In this decision, the Court concluded that the Ombudsman's decision did not exceed the scope of discretion granted to the Ombudsman under the FSMA 2000 nor violate the UK common law. In addition, the Court dismissed the financial service provider's claim for judicial review, deciding that the discretion granted under the FSMA 2000 and the fact that the Ombudsman did not hold an oral hearing in public did not violate the principle of the rule of law or the constitutional rights of the financial service provider.

Set forth below in length is a summary of the facts of the case and Ombudsman's decision, and of those issues before the Court which have been selected as being relevant to the subjects discussed in this article, and the decision and opinions of the Court on such issues. It has been prepared largely by use of excerpts from the decision of the UK Court of Appeals, with some short explanatory descriptions inserted at my discretion instead of giving the full text of the responding part of the court decision. While the summary has been prepared with a view to presenting those materials which would be useful in considering the standards of judgment for dispute resolution by Financial ADR in Japan, other valuable suggestions would be found in this court decision. Readers of this article are encouraged to read the entire text of the court decision.

The facts:

[62] *Heather Moor*, EWCA Civ. 642, *supra* note 4, at [19].

(a) HME's advice to Mr. Lodge

1. Heather Moor & Edgecomb Limited (hereinafter referred to as "HME") are independent financial advisers and gave advice to Mr. Simon Lodge in 1999. He was then aged 55 and was employed by British Airways as a pilot. He was approaching compulsory retirement from that employment, but he was intending to continue to work as a pilot for Airtour until aged 60. He was married with two children. His wife was significantly younger than him.[63]

2. Mr. Pickering of HME advised Mr. Lodge to leave the BA pension scheme on his retirement and to invest the proceeds in a section 32 pension plan with his fund invested in equities. In his letter to Mr. and Mrs. Lodge dated 21 June 1999, Mr. Pickering stated, " ... His pension fund would have gone up to somewhere around £730,000 minimum based on 9% per annum growth which I believe is very modest." "I have to say that I would consider it illogical not to take up the option ... I cannot see that there is any sound reason not to elect for the Section 32 Buy Out Plan."[64]

3. On 28 June 1999 Mr. Lodge signed an election to opt out of the British Airways Pension Scheme and to transfer his pension fund to a Section 32 plan with AXA Sun Life. Mr. Pickering made a note of that meeting that was typed on 30 June 1999.[65]

4. Mr. and Mrs. Lodge were not entirely comfortable with Mr. Pickering's advice. They consulted another independent financial adviser, Mr. Cooper. Following his meeting with them, in his letter to them of 7 July 1999, he reiterated his view that some of Mr. Pickering's comments breached the guidance issued by their regulator. By way of example, he referred to the assumption of 9% growth, which Mr. Cooper considered to be "anything but modest," and he stated that the PIA (the Personal Investment

[63] *Id.* [3].

[64] *Id.* [4].

[65] *Id.* [5].

> Authority, the then Regulator) had "recently introduced lower investment growth assumptions that have to be used by all life offices and advisers when projecting pension benefits."[66]
>
> 5. Mr. Lodge sent Mr. Pickering a copy of Mr. Cooper's letter. In Mr. Pickering's letter of 9 July 1999, he repeated his advice that the section 32 scheme was appropriate, and that a 9 per cent per annum assumed growth rate was "anything but modest." Ultimately, Mr. Lodge accepted Mr. Pickering's advice.[67]
>
> 6. Unfortunately, the assumed growth rate of 9 per cent per annum was not achieved. By letter dated 20 October 2003, Mr. Lodge informed HME that he felt obliged to claim compensation from them. His pension fund had in fact fallen in value by some 23 per cent. He calculated that he required a sum of over £340,000 to obtain the benefits he would have had if he had remained in the BA Pension Scheme. By letter dated 23 October 2003 HME rejected his complaint.[68]

(b) The complaint to FOS and the decision of Ombudsman

> 7. Following HME's rejection of his complaint, Mr. Lodge complained to the FOS. His complaint form was dated 11 November 2003.
>
> 8. By letter dated 18 November 2003, FOS sent a copy of the complaint form to HME and asked for copies of relevant documents from its file and "any evidence you wish us to take into account when considering this case." By letter dated 3 December 2003, HME sought the dismissal of the claim without consideration of the merits. In a further letter dated 2 February 2004, Mr. Pickering enclosed a copy of HME's file and gave a "detailed outline" of HME's case.[69]

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[66] *Id.* [6].

[67] *Id.* [7].

[68] *Id.* [8].

[69] *Id.* [10].

9. David Oliver, an adjudicator in FOS, by letter dated 7 April 2004, gave his opinion on Mr. Lodge's complaint. He set out the circumstances in which Mr. Lodge had been advised by HME, referred to HME's letters of advice, made a number of relevant findings and came to the following conclusions: his findings and conclusions cited by the Court include the following:

"In making a recommendation to transfer, I would expect clear evidence that the differences had been explained. This would include the advantages and disadvantages as well as setting out compelling reasons for the transfer. Mr. Lodge had indicated that he was prepared to accept a medium amount of risk with the investment of the transfer value. However, the funds that you recommended did not [meet] your definition of medium risk and there is no evidence that Mr. Lodge was aware of, or prepared to accept, the higher risk associated. The transfer and the investment funds you recommended may, therefore, have been unsuitable. I recommend that you carry out a loss assessment in accordance with the Pension Review methodology. If a loss is found to exist then redress should be paid in accordance with the Pension Review guidance. Please let me know no later than 21 April 2004 if you are prepared to make such an offer to Mr. Lodge. If you are unable to reply fully by then, please tell me how – with reasons."[70]

10. HME rejected Mr. Oliver's opinion. Their substantial response was enclosed with a letter dated 6 August 2004. Their response addressed the substantive issues, but it also contended that, (1) since the claim greatly exceeded the maximum amount [of £100,000] that FOS could require a firm to pay to a complainant, fairness required that it be determined by litigation in court, and that FOS should therefore decline jurisdiction, and (2) if that was not accepted by FOS, a hearing was requested so that disputes of fact could be resolved after hearing the witnesses.[71]

[70] *Id.* [11].

[71] *Id.* [12].

11. By letter dated 14 October 2003, Mr. Oliver responded to the procedural points raised by HME. (1) He stated that the financial limitation on the powers of FOS did not prevent them from considering Mr. Lodge's complaint. (2) In relation to the request for a hearing, he said:

"A hearing can be helpful where the documentary evidence produced by both sides is contradictory. Mr. Lodge has not produced any evidence that is considered contradictory and we do not, at this time, believe that a hearing would be advantageous."[72]

12. Following further correspondence, in which HME made further representations, Mr. Oliver adhered to his findings, and stated that unless there were grounds for a hearing, he would place all the evidence before an ombudsman for a final decision. In their letter of 1 July 2005, HME gave their reasons for seeking a hearing:

"Since this firm's "civil rights and obligations" are affected, we believe that we are entitled to a hearing, and, indeed, a public hearing – see Article 6 of the European Convention on Human Rights. If The Financial Ombudsman Service does not accept that primary contention then in the alternative we say as follows. We are unclear whether Mr. Lodge and Mr. Ross now accept the factual evidence which we have presented, in particular accounts that we have given at meetings with Mr. Pickering. If they dispute our evidence then a hearing is needed at which they can be cross-examined by counsel, and of course, at which our witnesses can also be cross-examined. We therefore suggest that The Financial Ombudsman Service ask Mr. Lodge and Mr. Ross whether they are prepared to accept our evidence."[73]

13. Tony King, one of the ombudsmen, wrote to HME on 11 July 2005. In relation to the request for a hearing, he stated:

"The Article 6 requirement does not have to be satisfied ... at every stage of the process of

[72] *Id.* [13].

[73] *Id.* [14].

determining "civil rights and obligations." The right to a hearing by way of judicial review of the Financial Ombudsman Service's decision remains open to you after you have received an ombudsman's decision. If you were right then a hearing would be required (if requested) in every case that reached the Financial Ombudsman Service. It is, I think, clear that more is needed than just that the case concerns civil rights and obligations.

"At present it is not clear that there is a dispute about what was said at meetings or, if there is, whether the case would turn on resolving what was in fact said.

"But if it was necessary to decide between disputed accounts, it does not follow that it would be necessary for witnesses to be heard in person or be cross-examined. The Financial Ombudsman Service has inquisitional powers. It may be that the dispute can be resolved by reference to other facts - rather than by testing the credibility of the witness. Even where held, oral hearings are intended to be informal and the procedure is set by the Ombudsman concerned. It is uncommon for there to be formal cross-examination. In the event of such a dispute I am not satisfied of the need for cross examination nor for a hearing."[74]

14. FOS issued a provisional decision on Mr. Lodge's complaint on 17 February 2006. The Ombudsman dealing with Mr. Lodge's complaint, Adrian Hudson, gave extensive reasons for his conclusions, and stated that subject to any further evidence or comment he intended to uphold the complaint and to make an award which, in substance, was the same as that finally made and summarized [below].[75]

15. Mr. Pickering responded to the provisional decision in a 21-page letter. It enclosed a witness statement signed by Anthony Marston-Smith, which had previously been provided unsigned. Mr. Marston-Smith was a financial adviser of long standing. He stated that there was "a respectable school of thought amongst investment advisers in November 2000 which would have considered it appropriate to quote future growth at 9%," and that "some competent

[74] *Id.* [15].

[75] *Id.* [17].

advisers would have recommended that Mr. Lodge make a transfer..."[76]

16. On November 26 2006, the Ombudsman then made his final decision below. He referred to paragraph 3.8.1 of the FOS Rules (Opinion as to fairness and reasonableness) and stated, "while I have taken into account the relevant law, I have determined this complaint based on what, in my opinion, is fair and reasonable bearing in mind all the circumstances of this case."[77]

[76] *Id.* [18].

[77] *Id.* [19].

The directions and recommendations of the Ombudsman:

> The Ombudsman directed that:
>
> > (1) HME arrange an assessment of Mr. Lodge's loss resulting from his acceptance of HME's advice.
> >
> > (2) HME pay the amount of that loss up to the sum of £100,000 (namely the maximum sum that the Ombudsman may direct be paid by a firm).
>
> The Ombudsman recommended that:
>
> > (1) if the amount of Mr. Lodge's loss determined in accordance with the decision exceeded £100,000 HME should pay the balance into his current pension arrangements.[78]

The grounds for the decision of the Ombudsman:

> 1. Mr. Lodge was willing to accept a medium degree of risk. The risk associated with the transfer was significantly higher than medium. The facts that were considered include: (1) Mrs. Lodge was significantly younger than Mr. Lodge. The large age difference would have been reflected in the cost of buying an annuity that included a spouse's benefits. (2) The transfer value represented a very significant proportion of Mr. and Mrs. Lodge's overall wealth. A competent adviser would have looked at the potential requirement for any widow's pension to have been paid for a significant period and the benefits payable on late retirement from the BA pension scheme and compared those with the projected benefits from the Section 32 Buy Out Policy.[79]
>
> 2. Ombudsman was not persuaded that Mr. Lodge would have decided to transfer his benefits if he had been provided with projections showing the benefits that might be provided by the scheme, if he deferred taking his benefits to age 60.[80]
>
> 3. If a projection showing benefits based on the new lower assumed growth rates set by the regulator had been shown to Mr. Lodge, he would have had cause in 1999 to consider that

[78] *Id.* [1].

[79] *Id.* [20].

[80] *Id.* [21].

the advice to transfer exposed him to a greater degree of risk than he had understood from the HME's comment on the projected growth after the transfer.[81]

4. Concerning the issue as to whether the advice was consistent with good industry practice in 1999, good industry practice in 1999 would have been to recommend against transfer in the particular circumstances of this case. In January 1999, the regulator issued instructions for firms to alter the assumed growth-rates used in projections, from a range with a mid-rate of 9% to a range with a new lower mid-rate of 7%. All firms were required to adopt the use of the new rates by 1 July 1999. However, in its letter of 9 July 1999, HME provided no projections on the reduced mid-rate and restated that assumed growth of 9% was modest.[82]

5. The loss of the value of the widow's pension that would have been paid by the BA pension scheme in the event of Mr. Lodge's death would, in any case, have undermined any perceived increase in the potential death benefits resulting from the transfer.[83]

The contentions of HME:

1. Section 228 of the FSMA 2000 requires that the Ombudsman determine complaints in accordance with the law.

2. Construction of the Act is required in order to avoid an infringement of the HME's Convention rights under Article 6 and Article 1 of the First Protocol ("A1P1").

3. The Ombudsman's decision departed from the rule of common law regulating requirements in determining liability for negligence of a professional. In short, a professional man is not to be held negligent if what he did was in accordance with the practice accepted by responsible persons in his profession (Bolam v Friern Barnet Hospital Management [1957] 1 WLR 582).

4. In any event, the Ombudsman should have held an oral hearing in public which would have allowed for cross-

[81] *Id.* [22].

[82] *Id.* [23].

[83] *Id.* [24].

examination by counsel. A1P1 protects property rights by the requirement of law for depriving of such rights and Article 6.1 of the Convention requires a fair and public hearing and public judgment.

The decision of the Court on the aforementioned contentions:

> 1. Section 228(2) does not require a complaint to be determined in accordance with the law. Ombudsman is free to depart from the common law standards in reviewing advice that is alleged to have been negligent or unsuitable, provided he complies with section 228 of the FSMA 2000.[84]
>
> Other provisions of the Act reinforce this conclusion. An award under section 229(2) (a) is not of the amount of the respondent's liability to the complainant, but again of the amount that "the ombudsman considers fair compensation for loss or damage. ...Paragraph (b) of section 229(2) explicitly confers [upon the Ombudsman the] power to make an order that a court could not make.[85]
>
> The following, taken from a decision in 2005, is referred to in the court decision.[86]
>
> > The words "in the opinion of the ombudsman" themselves make it clear that he may be subjective in arriving at his opinion of what is fair and reasonable in all the circumstances of the case. Of course, if his opinion as to what is fair and reasonable in all the circumstances of the case is perverse or irrational, that opinion, and any determination made pursuant to it, is liable to be set aside on conventional judicial review grounds."
>
> Thus, subjectivity is permitted. If the Ombudsman's opinion is "perverse or irrational" then conventional judicial review grounds will apply and the Ombudsman's opinion will be set aside. "Perverse or irrational" would be what we call in Japanese "Jyo-Shiki Hazure," which could be literally translated into "beyond or out of common sense".[87]

[84] *Id.* [40].

[85] *Id.* [37].

[86] *The Queen on the Application of IFG Financial Services, Ltd. v. Financial Ombudsman Services, Ltd.*, [2005] EWHC 1153 (Admin) (appeal taken from Eng.).

[87] In connection to this, Article 68 of the UK Arbitration Act 1996 allows the parties in arbitration to object in court against arbitral award on the grounds of "serious

> 2. As Section 228 should be literally read as stated above, the FOS scheme established under the FSMA 2000 satisfies the requirements of "law," and satisfies the requirements of Article 6 and A1P1 and the principle of the Rule of Laws.
>
> The Rule of Law is undoubtedly a basic principle, perhaps the basic principle, of our unwritten constitution and of the Convention. In "The Rule of Law" published in 2007, Lord Bingham emphasized the importance of the law being "accessible, and so far as possible intelligible, clear and predictable." Professor Paul Craig, in his paper on the Rule of Law appended to the Report of the Select Committee of the House of Lords, referred to the importance of the law being "capable of guiding one's conduct in order that one can plan one's life," and of clarity as to the consequences of breach of the rule of law.
>
> So far as Convention jurisprudence is concerned, the judgment of the Court in *The Sunday Times v. U.K.* raised the following two requirements.[88] Firstly, the law must be adequately accessible: the citizen must be able to have an indication that is adequate in the circumstances of the legal rules applicable to a given case. Secondly, a norm cannot be regarded as a "law" unless it is formulated with sufficient precision to enable the citizen to regulate his conduct...the law must be able to keep pace with changing circumstances. Accordingly, many laws are inevitably couched in terms which, to a greater or lesser extent, are vague and whose interpretation and application are questions of practice. *The FSMA 2000 satisfies these requirements.*

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irregularity" which affected arbitral tribunal, arbitral procedures, or arbitral awards, and enumerates nine grounds as a basis for judgment: (a) the arbitrators' failure to comply with the general duty to provide fairness and promote efficiency; (b) the arbitrators' excess of powers (otherwise than by exceeding substantive jurisdiction (separately provided in Article 67)); (c) the arbitrators' failure to conduct the proceedings in accordance with the procedure agreed by the parties; (d) the arbitrators' failure to deal with all the issues; (e) an excess of powers (vested by the parties) by an arbitral or other institution or person (other than the arbitrator); (f) uncertainty or ambiguity as to the effect of the award; (g) an award obtained by fraud or contrary to public policy; (h) failure to comply with the requirements as to the form of the award; or (i) any irregularity in the conduct of the proceedings or in the award which is admitted by the tribunal or arbitral institution. While some of these paragraphs, such as (a), (f), (g) and (i), provide for the grounds concerning the standards of judgment, the phrase "perverse or irrational" as used in the decision seems to permit a broader discretion than the standards of Article 68.

[88] *The Sunday Times v. The United Kingdom*, 6538/74 Eur. Ct. H.R. (1979).

3. Ombudsman is free to depart from the common law. Leaving aside that issue, Ombudsman clearly had the Bolam test in mind to take it into account in deciding what was fair and reasonable in the circumstances of the case. The rule set forth in Bolam case is subject to the qualification formulation in *Bolitho v City and Hackney Health Authority*.[89] In short, it further requires that the experts have directed their minds to the question of comparative risks and benefits and have reached a defensible conclusion. It is right that the Ombudsman applied the rule in Bolam and concluded that this did not satisfy the Bolam test, let alone Bolitho.[90]

4. The Ombudsman may consider whether oral evidence should be heard and whether a public hearing is required and the decision is subject to the judicial review. No unfairness is seen in the present case in the Ombudsman's decision that the evidence should be entirely written.[91]

In his supplementary comment, Lord Justice Rix recommended that the FOS should (i) select and publish suitable decisions in full, but anonymised, form in FOSBOOK, to show the relationships between. the broad principles applied to resolution of categories of cases and their application in practice; (ii) commission and publish regular academic analysis of the full range of Ombudsman decisions alongside future independent reviews. He also stated it is possible to see in the "fair and reasonable" jurisdiction of the Ombudsman the source not merely of an alternative dispute resolution service but of an important new source of law.[92]

[89] *Bolitho v City and Hackney Health Authority*, [1998] 1 A.C. 232 (H.L) 235 (appeal taken from Eng.).

[90] *Heather Moor*, EWCA Civ. 642, *supra* note 4, at [54]-[55].

[91] *Id.* [61]-[62], [66].

[92] *Id.* [85].

B. FIN-NET and INFO Network

The financial ADR system in the UK seems to play an important role in the expansion of financial ADR systems internationally.

A financial ADR system which seeks to ensure the reliability of financial markets to their consumers must be a financial ADR system that deals with cross-border markets. FIN-NET (Network for settling cross-border financial disputes out of Court) was established in 2001 in response to the integration of financial retail markets in Europe. Using the network of financial ADR organs, customers can make a complaint against a foreign financial service provider and pursue its resolution by contacting the dispute resolution scheme of their home country in their language and by virtue of its coordination with the financial ADR organ of that foreign country.[93]

International Network of Financial Ombudsman Schemes (herein referred as "INFO Network") is an association established in 2007 with the participation of financial ADR bodies from around the world. The objective of INFO Network is to enhance and develop financial ADR schemes through the exchange of technical information and experience among members. It is expected that designated dispute resolution institutions in the financial ADR system of Japan would be able to become its members and seek improvement and development of dispute resolution practice by financial ADR through exchanging information with members in other countries.[94]

V. THE STANDARDS OF JUDGMENT FOR DISPUTE RESOLUTION IN THE FINANCIAL ADR OF JAPAN

Section III discussed the standards of judgment for dispute resolution in *general* ADR. In Section V, I will now seek to clarify the standards of judgment for dispute resolution in *financial* ADR of Japan.

A. The Purpose of the Financial ADR System

[93] Regarding FIN-NET, see Financial Dispute Resolution Network at http://ec.europa.eu/internal_market/fin-net/index_en.htm. Also, as to the cases presented at the FIN-NET 2007 meeting in London, see Shuji Yanase & Shigehito Inukai, *Financial ADR and Ombudsman System*, *in* 3 ARBITRATION AND ADR FORUM (Japan Association of Arbitrators) (2010). In Case 1 the subject of the discussion was the contents of the Ombudsman's decision to admit the bank's liability for excess lending to the aged couple and provide a relief to the borrowers from their monthly repayment obligations resulting from the excessive lending.

[94] As to INFO Network, see International Network of Financial Services Ombudsman Schemes at http://www.networkfso.org/. With respect to a proposal to redesign the financial ADR in the United States, see Daniel Schwarz, *Redesigning Consumer Dispute Resolution: A Case Study of the British and American Approcahes to Insurance Claims Conflicts*, 83 TUL. L. REV. 735 (2009).

1. "Purpose" Provisions of Laws Regulating Financial Services Subject to the Financial ADR System

The financial ADR system was created with the revision of the 17 financial service industry laws by the addition of provisions concerning "designated dispute resolution institutions" to each of the industry laws. The financial ADR system should aim at contributing to the purpose of its founding laws, namely the Financial Instrument and Exchange Act and other laws regulating financial service industries. Such purpose is stipulated in Article 1 of each of such laws. Reviewing the purpose provisions of these laws reveals two findings:

First, the "purpose" provisions refer to the "public nature of business" of the respective financial services,[95] and some include the purpose to "ensure sound and appropriate operations of the business,"[96] to "secure proper operations of the business,"[97] to ensure the "fairness" of transactions,[98] or to "aim at fair price formation."[99]

Second, the "purpose" provisions stipulate that the purposes include maintaining credibility and facilitating the "protection" of customers.[100]

There are no provisions stipulating the purpose of the financial ADR system among the provisions related to the "designated dispute resolution institutions." Therefore, the purpose of the financial ADR system must be inferred from the aforementioned "purpose" provisions of the financial business industry laws. Thus, it could be understood that the purpose of the

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[95] *See, e.g.*, Financial Instruments and Exchange Act, *supra* note 6, art. 1; Shinyō kinkohō (信用金庫法) [Shinkin Bank Act], Act No. 238 of July 15, 1951, art. 1, *available at* http://law.e-gov.go.jp/htmldata/S26/S26HO238.html; Chōki shinyō ginkōhō (長期信用銀行法) [Long-Term Credit Bank Act], Act No. 187 of July 20, 1952, art. 1, *available at* http://law.e-gov.go.jp/htmldata/S27/S27HO187.html; Ginkōhō (銀行法) [Banking Act] Act No. 59 of July 1, 1981, art. 1, *available at* http://law.e-gov.go.jp/htmldata/S56/S56HO059.html; Hokengyōhō (保険業法) [Insurance Business Act], Act no. 105 of July 7, 1995, art. 1, *available at* http://law.e-gov.go.jp/htmldata/H07/H07HO105.html.

[96] *See* Banking Act, *supra* note 95, art. 1.

[97] Teitō shōken gyō no kisei tō ni kansuru hōritsu (抵当証券業の規制等に関する法律) [Act on Regulation, etc. of Mortgage Securities Business], Act No.114 of 1987, art.1 (amended 2006) [hereinafter Mortgage Securities Business Act], *available at* http://law.e-gov.go.jp/haishi/S62HO114.html.

[98] *See* Financial Instruments and Exchange Act, *supra* note 6, art. 1; Insurance Business Act, *supra* note 95, art. 1; Shintaku gyōhō (信託業法) [Trust Business Act], Act No. 154 of 2004, art. 1 (amended 2012), *available at* http://law.e-gov.go.jp/htmldata/H16/H16HO154.html.

[99] *See* Financial Instruments and Exchange Act, *supra* note 6, art. 1.

[100] *See id.* art. 1; Shinkin Bank Act, *supra* note 95, art. 1; Banking Act, *supra* note 95, art. 1; Insurance Business Act, *supra* note 95, art. 1; Trust Business Act, *supra* note 98, art. 1; Shikin kessai ni kansuru hōritsu (資金決済に関する法律) [Settlement Act], Act No.59 of 2009, art. 1 (amended 2009), *available at* http://law.e-gov.go.jp/htmldata/H21/H21HO059.html; Mortgage Securities Business Act, *supra* note 97, art.1.

financial ADR system is "in view of the public nature of business of the financial service industries, "to ensure sound and appropriate operations of the business," "to aim for fair price formation by ensuring the fairness of transactions," and "to maintain the credibility of financial service industries in the people's mind and to facilitate the protection of customers."

2. The Government's Reasons for Proposing the Bill that Created the Financial ADR System

Before the financial committee of the House of Representatives and the financial committee of the House of Councilors, the government explained its reasons for introducing the bill to enact the Act for the Partial Revision of the Financial Instruments and Exchange Act, etc. and to create the Financial ADR system, as follows: "against the backdrop of the current turmoil in global financial and capital markets, it has become an important issue to facilitate the strengthening of market functions in Japan and to enhance user protection and construct financial and capital markets which are reliable and vital. Under these circumstances, this bill is submitted in order to create a system to meet these requirements." Explaining the system, the government further stated that "in order to enhance user protection, it is proposed to establish the alternative dispute resolution system in the financial field, the so-called financial ADR system, and to introduce the designation system of dispute resolution institutions and also to require financial institutions to fulfill an obligation to conclude a contract with designated dispute resolution institutions".[101]

The government acknowledges the necessity to enhance user protection in the financial and capital markets of Japan. It recognizes that enhancement of user protection by constructing reliable financial and capital markets is an important objective. Although no detailed explanation was given as to how the then existing system was insufficient for consumer protection, it is clear that improving the system and enhancing customer protection is one purpose of establishing the financial ADR system.

3. Supplementary Resolutions of the Committees and Supplementary Provisions of the Financial ADR System Founding Law

The financial committee of the House of Representatives and the financial committee of the House of Councilors made their respective supplementary resolutions when they passed the financial ADR system founding law.

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[101] The motivation and reasoning of the Japanese government can be found in the minutes of the treasury and finance committee. Minutes of the Finance Committee of the House of Representatives no. 14 (財務金融委員会第 14 号), 171st Diet of Japan (April 8, 2009), *available at* http://kokkai.ndl.go.jp/SENTAKU/syugiin/171/0095/17104080095014a.html.

The supplementary committee resolution of the House of Representatives (April 22, 2009) stated that the government should give due regard to the following matters concerning the financial ADR system: (i) facilitating the cross-industry efforts among industry associations towards the establishment of a cross-industry and comprehensive dispute resolution institution in the financial field, (ii) ensuring the mutual collaboration of designated dispute resolution institutions, (iii) collecting, analyzing, and summarizing information about complaints and disputes regarding financial products or services and information concerning dispute resolution and other business of designated dispute resolution institutions, and promoting the sharing of the results among related institutions, such as designated dispute resolution institutions, the National Consumer Affairs Center of Japan, and the Japan Legal Support Center and encouraging closer mutual collaboration among related parties.[102]

The supplementary committee resolution of the House of Councilors raised the points similar to items ii) and iii) above.

In addition, Article 21 of the supplementary provisions of the financial ADR system founding law stipulates that within three years of the enactment of the law, the government "shall examine the system for alternative dispute resolution by designated dispute resolution institutions, including the desirable manner of involvement of the Consumer Affairs Agency and the feasibility for a cross-industry and comprehensive dispute resolution system and, if it is considered necessary, shall take such measures as the result of the examination may require."[103]

It should be noted that these supplementary resolutions and supplementary provisions did not address at all the questions about the financial ADR system's position within the broader judicial system. These issues include: the standards of judgment for dispute resolution in financial ADR, the scope of authority, the degree of discretion granted to the designated dispute resolution institutions, and how the courts shall deal with the "special conciliation proposal" and the procedures taken by a designated dispute resolution institution or their adjudicators.

B. Unique Features of the Financial ADR System

I would like to further clarify the purpose of the financial ADR system by examining some unique features of the financial ADR system. This examination may raise some issues concerning interpretation of the law that may have to be addressed further in the future or raise issues that may lead to discussion of modifying the present financial ADR system. Recognition of such

[102] Minutes of the Finance Committee of the House of Representatives no. 20 (財務金融委員会第20号), 171st Diet of Japan (April 22, 2009), *available at* http://kokkai.ndl.go.jp/SENTAKU/syugiin/171/0095/17104220095020a.html.

[103] *Id.*

unique features is expected to be useful in clarifying the purposes of the financial ADR system.

1. Importance of the Financial ADR System

The financial system forms the basis of the economy of modern society. Funds indispensable for economic activities are supplied through financial networks. If the flow of funds is disrupted, the economy itself suffers serious damage. This is obvious from the fact that the financial crisis of 2008 originated from the United States of America, but later caused serious economic problems to developed countries, such as high unemployment.

2. Unique Features of Financial Products and Financial Services

Financial products and financial services are not tangible goods and their value is accepted only when they are credible.

They are generally complicated and are subject to constant innovations and, being cross-border in nature, they are subject to influences across multiple borders. Specialized knowledge is necessary to know and understand their contents. Whether they will produce a result as expected cannot be immediately known. In addition, time being an important factor for financial products or financial services, resolutions of complaints or disputes concerning financial products or financial services cannot be satisfactory to customers unless they are prompt.

Financial products and financial services which are the subject of the financial ADR system have these unique aspects.

3. The Financial ADR System as Infrastructure for the Financial System

The public's trust in financial services is the basis of any financial system. The financial system cannot survive without the public's trust. The financial ADR system has the following two administrative purposes: (i) providing easy, prompt, and appropriate relief of customers, and (ii) by doing so, maintaining the public's trust in financial services and seeking to establish the infrastructure of financial system.

Article 2 of the Consumer Basic Act confirms that "relief" is a consumer right, but it stipulates only that the relief shall be "appropriate and prompt" when "damage is incurred."[104] In case of "relief" by financial ADR, its contents should be determined in accordance with socially accepted conventions or common sense with respect to what the financial services ought to be in order to secure the public's trust.

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[104] Consumer Basic Act, *supra* note 9, art. 2.

Thus, although the financial ADR system was founded to address two separate administrative purposes, consumer protection should be achieved by shaping financial services into what they ought to be. We should exert our efforts to realize an ideal financial ADR system, with the clear intention and purpose of establishing it as the infrastructure of the financial system. As a result of such efforts consumer protection will be realized. The standards for judgment in financial ADR should be examined with a clear understanding of this relationship of the two administrative purposes.

The role of the financial ADR system is not limited to providing relief to individual customers. The financial ADR system is expected to immediately call public attention to the problems behind the contents of or methods of selling financial products or financial services through customer complaints, and prevent the recurrence of such problems with the goal of normalizing financial services.

4. Application of the Principle of Customer Protection

Is it necessary to provide protection or redress to customers who buy financial products or financial services, to the same extent as employees aggrieved by employers, or consumers suffering physical damage or loss of life due to unsafe food are provided?. One could argue that financial products or financial services are luxuries and not indispensable for existence so that protecting consumers against infringement of their rights is enough and "relief from damages or loss" is unnecessary.

Where customers suffer harm due to inappropriate services of financial service providers, it is unfair that the financial service providers escape any consequences and retain the compensation for such services as if the services were appropriate. Moreover, if inappropriate financial products or financial services cause harm to the *average* livelihood of those people, it would be socially inappropriate to leave such harm without redress or relief. Individual financial assets should be protected in the same way worker's rights or food safety in a modern society is protected when the financial assets are necessary to support their stable lives in future years.

Also, it is clear that Articles 1 and 2 of the Consumer Basic Act are generally applicable to customers of financial service providers.[105] Between financial service providers and customers "there is a discrepancy in the quality and quantity of information and negotiating power" as provided in Article 1 of the Act and customers should benefit from Article 2 of the Act, which provides as one of the customers' rights that they "be provided with easy, prompt, and appropriate relief when damages are incurred."

However, the amount in dispute concerning the financial products or financial services can be extremely high. Financial ADR aims to provide easy, prompt, and flexible relief for customers without using the judicial process, and therefore it seems to be reasonable to limit the use of financial ADR to a

[105] *Id.* arts. 1–2.

certain amount. When considering the purpose of financial ADR, certain disputes that exceed a certain monetary amount should be resolved through arbitration or court proceedings and should be excluded from financial ADR. The limit should cover such range of financial services as would be necessary to satisfy the purpose of the financial ADR system to maintain the public's trust in financial services. There currently is no limit on the amount that may be disputed in the existing financial ADR system and the existing laws leave customers to determine whether to use financial ADR or not. As a result, financial service providers bear a burden under the existing scheme.

In addition, the Consumer Basic Act refers to "consumers" and "service providers" who are to confront each other, but does not define "consumer" in the context of the Act. The "Consumer Contract Act," which was also enacted to protect the interests of consumers, defines "consumer" an individual (excluding individual party to a contract made in the course of, or for the purpose of, his business).[106] In the context of financial ADR, it remains difficult to reasonably determine whether a customer should be protected or not under the definition set forth above. Receivers of financial services are not limited to individuals, and financial services are often important in the course of business. When considering the financial ADR system's purpose of maintaining the public's trust, no one would reasonably conclude that these cases should be excluded from the protection provided by financial ADR.

Given these perspectives, the financial ADR system should be understood and designed as part of the infrastructure of financial system to provide a system of resolving complaints or disputes, up to a specified amount, of those customers who have received financial services, rather than as a system for protection of "consumers" as generally provided in the consumer protection legislation. It is clear, however, that the provisions of financial products or financial services shall not breach any legislation to protect consumers.

5. The Administrative Purpose of the Financial ADR System

The financial ADR system is a part of the infrastructure of the financial system. It is therefore an alternative dispute resolution system which is subject to the supervision by the administrative government responsible for the development of this infrastructure. Accordingly, the purpose of the financial ADR may also include carrying out administrative needs.

Alternative dispute resolution systems in Japan can be classified into several types. Based upon the organizations which undertake the responsibility for their management, they can be classified into the following three categories: (i) "Court Administered ADR," (ii) "Private Institution ADR," and (iii) "Administrative Government ADR." As their names indicate, (i) is conducted with the participation of judges, and (ii) is carried out by private ADR institutions, which may include "certified private ADR institutions" authorized by the Ministry of Justice pursuant to the ADR Promotion Act. The

[106] *Id.* art. 2(1).

"Administrative Government ADR" in (iii) above is conducted by a relevant administrative office or agency either independently or with the participation of those appointed by them.[107]

Alternative dispute resolution systems could also be classified into (i) ADR systems aimed solely at resolution of disputes and (ii) ADR systems aimed at not only resolution of disputes, but also fulfilling specified administrative purposes. The former can be referred to as "Judicial ADR" and the latter can be referred to as "Administrative Purpose ADR." Using this classification, the financial ADR system can be both "Private Institution ADR" as well as "Administrative Purpose ADR."

6. Collection, Analysis, and Sharing of Information under Financial ADR and the Obligation of Confidentiality – The Necessity for Two Contradictory Requirements

Since financial ADR is an "Administrative Purpose ADR," designated dispute resolution institutions are required to collect and analyze information available to them and share the result of their analyses with the relevant administrative bodies, and disclose it to the public. While the privacy and confidentiality is generally regarded as one of the *general* ADR's characteristics and merits, financial ADR diverges from this characteristic.

Financial ADR deals with the question of what is desirable of financial services. This is an important issue for the people of the nation at large, and at the same time a material concern for financial service providers. Complaints and disputes before the financial ADR system involve individual customers but, when put together, become a matter of public interest. For these reasons, the principle of confidentiality will have to be altered to allow for the collection, analysis, and sharing of information available to financial ADR institutions, to the extent it is necessary. Through this information sharing, the standards of judgment for financial ADR will be subject to criticism and gradually become clearer, which increases the predictability of outcomes for the related parties.

Article 156-41 of the FIEA stipulates that adjudicators, officers, and employees of designated dispute resolution institutions are obligated to maintain the confidentiality of any information obtained during the course of

[107] The consultation and mediation procedures for individual labor disputes by the Labor Bureau, and the adjustment procedures (mediation, conciliation, and arbitration) for labor disputes (both collective industrial disputes and individual labor disputes) by the Labor Relations Commission fall under "Administrative Government ADR," and the Labor Tribunal Procedure is a "Court Administered ADR." Dismissal decisions or Orders of the Labor Relations Commission are administrative measures (or decisions) and as such is the subject of cancellation via a decision in a lawsuit under the Administrative Case Litigation Act. Courts retain the power to make final decisions. Gyōsei jiken soshōhō (行政事件訴訟法) [Administrative Case Litigation Act], Act. No. 139 of 1962 (amended 2011), *available at* http://law.e-gov.go.jp/htmldata/S37/S37HO139.html.

their duties, and, for the purpose of application of the Criminal Code and other penal provisions, they shall be deemed to be "officials engaged in public service pursuant to applicable laws and regulations."[108] This obligation of confidentiality shall be interpreted in harmony with Article 156-58, Paragraph 1, of FIEA, which authorizes the Prime Minister, if the Prime Minister deems necessary, to exercise the power to procure reports and conduct on-site inspection of designated dispute resolution institutions.[109] In interpreting the confidentiality obligation of Article 156-41, we must also consider that sharing information with the public is necessary for meeting the purpose of public interest discussed above. The obligation of confidentiality of Article 156-41 is stipulated for the benefit of the disputing parties with respect to their respective individual cases. Thus, subject to the constraint of confidentiality, the information must be used for the administrative and public purposes of the financial ADR system.

In recent years, the principle of confidentiality in international arbitration is under pressure for modification. Subject matters of international arbitration are expanding from commercial disputes to include disputes involving public interest. For example, investment treaty arbitrations involving national governments as respondents clearly implicate public interest. In cases of investment treaty arbitrations, not only are the people in the party countries affected, but also those who make investments relying on similar investment treaties are indirectly affected as they seriously consider such decisions when interpreting treaties. Thus, to enhance the predictability of such arbitration decisions, sharing information on precedents and disclosing the progress of such proceedings is necessary.[110]

[108] Financial Instruments and Exchange Act, *supra* note 6, art. 156-41.

[109] *Id.* art. 156-58.

[110] ICSID is an organization that handles international arbitrations under investment treaties. It publicizes information concerning arbitration conducted under it. This information is available at ICSID's website (http://icsid.worldbank.org/).

7. Relationship with the Court

Financial ADR seeks to resolve promptly and flexibly complaints of customers (consumers) of financial services. It aims at protecting customers and securing the public's trust in, and ensuring sound development and maintenance of, the financial system, which forms the basis of the modern economic system. Its purpose consists of the administrative purposes as set out above as well as protection of customers. It does not seek to make decisions in accordance with the "justice by law" but seeks to find "relief" of customers to satisfy such administrative purposes.

Given this perspective, it is now understood that dispute resolution by financial ADR is not entirely a matter within the judiciary system for which the court is responsible. While falling under the judicial field in its broader sense, the financial ADR system has such aspects as are subject to the jurisdictions of the administrative agency responsible for supervision of financial service providers and of the administrative agency responsible for consumer protection administration.

Dispute resolution in financial ADR cannot be completed so long as a settlement proposal or special conciliation proposal is not accepted by both of the disputing parties, namely financial service provider and customer. The dispute resolution is based on an agreement between both parties. Under the financial ADR system both parties are entitled to seek examination and judgment by the courts, irrespective of any judgment made by any financial ADR institution or adjudicators. If, because of this structure of the financial ADR system, the court should examine and make decisions as if there were no such proceedings taken by the financial ADR system, would that be consistent with the purpose of the financial ADR system? According to the existing financial ADR system founding law, the court is free to do so, while it may be possible for the court to benefit from the ADR proceedings by permitting the parties to present them before the court as evidence. Under the present system financial ADR procedure is isolated from court proceedings. Moreover, the court does not have the power to undertake "judicial review" of the "special conciliation proposal." There is no mechanism under which the court should examine the "special conciliation proposal." Whether to introduce such a mechanism is a question left to the legislature, which should be examined in light of the results of operations of the financial ADR system.

C. Accomplishments of the Standards of Judgment in Financial ADR Required by Disputing Parties and Others

Here I would like to examine the disputing parties' and other parties' needs of what in detail should be accomplished by the standards of judgment in financial ADR, taking into account the purpose of financial ADR (as discussed in Section (V)(A) above) and also the unique features of the disputes handled by financial ADR (as discussed in Section (V)(B) above). The standards of judgment in financial ADR will be required to satisfy the following needs:

1. Disputing Parties' Needs

If customers who are parties to financial ADR disputes do not accept the standards as being reasonable, the financial ADR system will end up as just an idea on paper without being used in practice. For the financial service providers who provide funds for management and operation of the system, the decisions should be convincing to them and the designated dispute resolution institutions should provide them with the merits of enabling them to maintain their customers' trust at large and to receive useful information for their business. In addition, in light of the purpose of the financial ADR system, the standards will have to be supported by the administrative agencies which have the regulatory power over the financial service providers.

2. Need for Authoritative Fact-finding

In order to make the judgment for dispute resolution in financial ADR authoritative to parties in dispute, the fact-finding by adjudicators should be satisfactory to them in the first place. Although it is desirable to have no conflict over the facts, parties often dispute over the facts of a case.

How to handle disputes over the facts is an important issue. It goes without saying that financial service providers' fairness and honesty about the facts is the indispensable premise of the people's trust in the financial ADR system. In Japan, are these conditions satisfied? Does suspicion prevail among the people that financial service providers may make customers put their personal seal on their printed documents having more detailed content than what their employees explain to the customers, in preparation for possible subsequent disputes? Should there be such suspicion, financial service providers must devise how to dispel such suspicions. For both parties, having an honest and fair attitude in their assertion of facts is the first step. Without it, the financial ADR system will never have the public's trust and it is useless to argue about the allocation of the burden among the disputing parties to establish the ideal financial service or about the standards of judgment for customer "relief." The standards of judgment for financial ADR shall be required to strongly urge both disputing parties to take a frank and honest attitude and bring it into practice during the fact finding process.

3. Need for Easy, Prompt and Flexible Judgment

Adjudicators are expected to consider flexibly the best procedures or settlement proposals. It is hoped that in doing so adjudicators will not depart from the law in many cases. However, it would be considered as appropriate in some cases to take simple procedures or make flexible settlement proposals which would be impossible in courts. In such cases, the adjudicators are required to make decisions, with reasons, freely and vigorously in order to

fulfill the purpose of the financial ADR system. Only in doing so, will the financial ADR system become a practically meaningful system that has the support of the public.

4. Need for Legitimate Judgment

In case of dispute resolution before the court, a dispute is, in general, presumed to be resolved in accordance with law if it is a court judgment, and presumed to be within the scope permissible to the court if it is a court-involved settlement despite the fact it is reached by agreement of the parties involved. Therefore, such dispute resolutions are generally accepted as legitimate, satisfying the requirements of "the rule of law" and "due process" for protection of rights.

Judgment made in "special conciliation proposal" must also be legitimate, satisfying the requirements of "the rule of law" and "due process." For this reason, certain questions will be asked with regard to such judgment. They are whether or not such judgment is allowed to depart from a result of application of statutory law or judicial precedent, to what extent such judgment is permitted to depart from such result in order to be accepted as legitimate, and for what reasons such judgment will be accepted as legitimate. The standards of judgment in financial ADR must properly reply to these questions and be accepted as legitimate.

D. Sources of Law for the Standards of Judgment in Financial ADR

Taking into consideration the sources of law for the standards of judgment in ADR in general as discussed in Section III above, I would like to go through the sources of law that formulate the standards of judgment for dispute resolution in the financial ADR in Japan. For this purpose also considered comprehensively are "A. the Purposes of the Financial ADR System," "B. the Unique Features of the Financial ADR System," and "C. the Accomplishments of the Standards of Judgment in Financial ADR Required by Disputing Parties and Others," all as discussed above in Section V.

It is obvious that the Civil Code, the Commercial Code, the financial service industry laws and other laws and various regulations thereunder are sources of law which are applied to the judgment for resolution of individual disputes in financial ADR. The assignment here is to seek such sources of law of judgment as should be further applied based on a result of application of such laws and regulations.

As has been hitherto observed, there are neither statutory laws nor rules squarely designed to establish the standards of judgment for dispute resolution in the financial ADR system. Such standards must be extrapolated from various sources of law. I would like to examine not only those provisions of statutory laws which are directly applicable to the standards of judgment and those which are interpreted to be applicable by analogy, but also soft laws guiding financial ADR practice (namely rules of private institutions as opposed

to national laws). In looking into the sources of law, I will also take into consideration the roles of designated dispute resolution institutions and their adjudicators in each stage of dispute resolution process in the financial ADR and the purposes and contents of their judgments required in each such stage, as described in Section (II)(B) above, as well as the proposition that the judgments concerning "special conciliation proposal" should provide guidance applicable through all stages of the financial ADR, as discussed in Section (II)(C) above.

1. Stipulations on Dispute Resolution in the FIEA and Other Financial Service Industry Laws

General standard of judgment

General standard of judgment for dispute resolution in the financial ADR can be extracted from the stated purposes of the financial ADR system (as discussed in Section (V)(A) above). It can be understood "to ensure the fairness in providing financial services to maintain credibility in the people's mind and facilitate the protection of customers."[111] In other words, we can state that the general standard of judgment is "to correct those financial services which do not provide sound, appropriate, and fair services and to provide relief for customers who were aggrieved by such financial services."

Conciliation criterion and decision criterion of "special conciliation proposal"

Article 156-44, Paragraph 2, Item 5 of the FIEA, provides two conditions for presentation of a "special conciliation proposal." The first is that there is "no chance of reaching settlement between the parties" and the second is that making the proposal "is considered suitable in light of the nature of the case, the intentions of the parties, the process of the proceedings taken by the parties and any other circumstances."[112] These requirements are similar to the conditions that Article 17 of the Civil Conciliation Act requires of the court when it makes an "order in lieu of conciliation." Article 17 of the Civil Conciliation Act provides, among others, that "when the court considers as appropriate in cases where there is no possibility for reaching conciliation, the court may make a decision necessary to resolve the case ... taking the equity of both parties into consideration and looking at all the circumstances."[113]

In interpretation of this Article 17 of the Civil Conciliation Act, it is understood that the decision criterion in civil conciliation is, as in the case of the conciliation criterion, the "fair and reasonable (*Jori*)" test (See Section (III)(B)(2) Article 17 [Decision in lieu of conciliation] above). Concerning the

[111] Financial Instruments and Exchange Act, *supra* note 9, art. 1.

[112] *Id.* art. 156-44.

[113] Civil Conciliation Act, *supra* note 1, art. 17.

conciliation criterion and the decision criterion in "special conciliation proposal," there is no reason to exclude the "fair and reasonable (*Jori*)" test from their standards of judgment.

In financial ADR, the purpose of the system will be incorporated into the "fair and reasonable (*Jori*)" test to be applied in financial ADR and such test will correct financial service providers' behavior and provide relief to customers.

2. The ADR Promotion Act[114]

Article 1 (Alternative Dispute Resolution Procedures)[115]

It is obvious that dispute resolution procedures of designated dispute resolution institutions for financial ADR must satisfy those elements which are stipulated in the definition of alternative dispute resolution procedures in Article 1 of the ADR Promotion Act. However, for the purpose of analyzing the standards of adjudicators' judgment, no particularly useful elements are found among the elements in the stipulated definition, that is "the procedures for resolution of civil dispute between parties who seek, with the involvement of a neutral third party, a resolution without using litigation procedure." It requires that an adjudicator shall be a "neutral third party," but this is a requirement for the attribute of "the third party," rather than stipulation of the standards of judgment, and it should be ensured by operating or other rules of designated dispute resolution institutions.

Article 2 (Private Dispute Resolution Procedures)[116]

In Article 2, Item 1 of the ADR Promotion Act, alternative dispute resolution procedures which private ADR institutions take, with respect to civil disputes, in mediation of settlement at the request of both parties to the dispute is defined as "Private Dispute Resolution Procedures." The preparation and recommendation of settlement proposals by adjudicators are included in "mediation of settlement" in the definition of "Private Dispute Resolution Procedures" in Article 2, Item 1, and, therefore, these procedures taken by designated dispute resolution institutions fall under the definition of "Private Dispute Resolution Procedures." By the provisory provisions of the same Item 1 and the Cabinet Ordinance thereunder, the conciliation procedures by the designated dispute resolution organ under the Compensation of Damages of Automobile Accidents Security Act and the mediation and conciliation procedures by the designated housing dispute resolution organ under the Housing Quality Assurance Act are excluded from this definition, but

[114] ADR Promotion Act, *supra* note 8.

[115] *Id.* art. 1.

[116] *Id.* art. 2.

mediation of settlement by designated dispute resolution institutions for financial ADR is not excluded from the definition of "Private Dispute Resolution Procedures."

As the alternative dispute resolution procedures taken by designated financial ADR institutions fall under the definition of "Private Dispute Resolution Procedures," a designated financial ADR institution is qualified for the application for issuance of the certificate of the Ministry of Justice to it under the ADR Promotion Act. The ADR Promotion Act is applicable not only to the certified private ADR institutions but also to other private ADR institutions conducting Private Dispute Resolution Procedures. Accordingly, it is obvious that, with or without such certificate of the Ministry of Justice, dispute resolution procedures of designated dispute resolution institutions are subject to the basic principle of ADR procedures stipulated in Article 3, Paragraph 1 of the ADR Promotion Act.

Article 3 (Basic Principle of Alternative Dispute Resolution Procedures)[117]

The basic principle and other provisions in Article 3 of the ADR Promotion Act are applicable to designated dispute resolution institutions for financial ADR. The basic principal in Paragraph 1 is applicable as the basic principle of the alternative dispute resolution procedures at the designated dispute resolution institutions and the obligation clause in Paragraph 2 is applicable to such institutions.

Accordingly, the procedures to prepare a settlement proposal and recommend it in financial ADR must be consistent with the basic principle of Article 3, Paragraph 1 of the ADR Promotion Act as discussed in Section (III)(B)(1) Article 3-1 (Basic principles of ADR procedures) above. According to the basic principle of alternative dispute resolution set forth in Article 3, Paragraph 1, the procedures for complaint handling and preparation and recommendation of a settlement proposal in financial ADR (i) must be such as can be characterized as "procedures for settling dispute by law." Being characterized as such, they must further (ii) "respect the disputing parties' voluntary efforts for dispute resolution," (iii) "be executed in a fair and appropriate manner," (iv) "based on specialized expertise" and (v) in such manner as "properly corresponding to the actual conditions of the dispute," and (vi) be aimed at finding "prompt dispute resolution."

Obviously whether adjudicator's judgment in the process of complaint handling or preparation and recommendation of a settlement proposal is consistent with this basic principle should be determined by reference to the question of whether the dispute resolution procedure in financial ADR itself can be regarded as "a procedure for settling dispute by law," without regard to the fact that the judicial judgment can be sought if the parties do not accept the "special conciliation proposal." Dispute resolution in financial ADR is ultimately made solely by agreement of disputing parties. Upon failure of such agreement "procedure for settling disputes by law" can be taken by the court.

[117] *Id.* art. 3.

This does not dispense with the requirement that ADR procedures prior to the litigation at court should satisfy this requirement.

Insofar as Paragraph 1 of this Article is concerned, it would be reasonable to understand that the requirements in (ii) through (vi) above grant adjudicators a broad discretion. The discretion is limited by the requirement in (i) above so that the procedures must be such as can be characterized as "the procedures for settling disputes by law." Adjudicators are permitted to make their judgment freely with a broad discretion on those directions listed in (ii) through (vi) above, so far as the procedures are determined as a whole to be the "procedures for settling disputes by law." The term "settling dispute by law" as used here does not mean resolution of dispute consistent with statutory laws or court precedents, but can be understood to mean "resolution of dispute satisfying the requirement of the rule of law." This is clearly established by the provisions of the laws concerning civil conciliation or arbitration, which are included in the alternative dispute resolution procedures as defined in the ADR Promotion Act. (See Section (III)(B)(2) and (3) above)

In the financial service industry, the content of financial products and financial services being dealt with cannot be understood without specialized expertise, and is subject to constant innovation. For these reasons, the regulatory authorities' supervisory standards and guidelines, relevant industry practice, and the relevant industries' codes of conduct and guidelines will provide important directions for determining whether procedures meet the requirements of "aiming at prompt dispute resolution based on specialized expertise and in such manner as properly responding to the actual conditions of the dispute," as set forth in (iv), (v) and (vi) above.

3. Application by Analogy of Articles 1, 17, and 14 of the Civil Conciliation Act[118]

The Civil Conciliation Act does not apply to the financial ADR as it is not civil conciliation conducted in the court. However, both civil conciliation and financial ADR are alternative dispute resolution procedures for the purpose of resolving disputes other than litigation procedures. Thus, it would be reasonable to take the position that the provisions of the Civil Conciliation Act concerning the criteria for conciliation and for decision made in lieu of conciliation can be applied *by analogy* to the standards of judgment in financial ADR. Among the ADR procedures in Japan civil conciliation is the form of dispute resolution which has been most frequently used, and there has been accumulation of experiences and examination with respect to the conciliation criterion and the decision criterion. These should provide valuable suggestions for considering the standards of judgment for dispute resolution in financial ADR.

[118] Civil Conciliation Act, *supra* note 1.

Article 1 and Article 17[119]

Article 1 of the Civil Conciliation Act stipulates that the standard of judgment for dispute resolution in conciliation shall be "fair and reasonable (*Jori*)" test. In addition, while Article 17 of the Civil Conciliation Act includes provisions requiring to take "the equity of both parties" in making the "decision in lieu of conciliation," it is understood that both the conciliation criterion to be applied before reaching this decision and the decision criterion to be applied to determine the contents of the decision are the "fair and reasonable (*Jori*)" test. The "fair and reasonable (*Jori*)" test cannot lead to a judgment which is in violation of any mandatory statutory provision but is not bound by any statutory provision (other than mandatory provisions) and, where there is no applicable substantive law, can lead to create new rights. The "fair and reasonable (*Jori*)" test must be identical to whatever standard as is objectively recognized as being consistent with "common sense." Since disputes which financial ADR handles may involve something technically advanced and new financial products or services, there may be some cases where the judgment made in such disputes is not necessarily recognized as being consistent with "common sense" prevailing in the society. In such cases it may be appropriate to describe the judgment as being required to be "in line with good sense" in the relevant financial service industry.

This "fair and reasonable (*Jori*)" test is nothing but the "law," which guides judgments in individual cases and such judgments will, when accumulated, shape the substance of rights. This idea is consistent with that of the common law of the Anglo-American jurisprudence. The alternative dispute resolution procedure is expected to help the formation of law by the "fair and reasonable (*Jori*)" test in the rapidly changing modern society.

Article 14[120]

Whether Article 14 of the Civil Conciliation Act should be applied *by analogy* to financial ADR is controversial. In case a designated dispute resolution institution or their adjudicators find that an agreement being reached between disputing parties is inappropriate, how should the case be handled? If the dispute is going to be resolved by agreement between the parties, is it impossible for the designated dispute resolution institution or their adjudicators to express that finding? In other words, should they interfere with contents of the agreement in such case, as they have an administrative role, as well as the dispute resolution role, to make the financial service industry become what it ought to be? In preparation of settlement proposals or special conciliation proposals by adjudicators, this issue can be avoided in many cases because they take the initiative in doing so. However, it seems that not all the cases can avoid this issue. In fact, even after a "special conciliation proposal" is presented, financial service providers may evade

[119] *Id.* arts. 1, 17.

[120] *Id.* art. 14.

being bound by such special conciliation proposal by the conclusion of settlement or conciliation made outside the same financial ADR procedure. Noting this point, one will take a view that the parties are free to resolve their dispute by their mutual agreement irrespective of its content and there is no possibility for adjudicators to intervene contents of the agreement. While it is unknown whether this issue will occur in the future practice of financial ADR in Japan, I would like to expect that this problem can be avoided by persuading the parties with full explanation.

4. Articles 36 and 45 of the Arbitration Act[121]

Article 36[122]

Based upon the parties' agreement to resolve their dispute by arbitration rather than resorting to the court, an arbitral award is rendered and, except for limited reasons as provided in Article 45, Paragraph 2 of the Arbitration Act, it ultimately binds the parties.[123] In contrast, dispute resolution by financial ADR is not resolution of dispute by arbitration. In financial ADR there is no agreement to arbitrate between the parties. The "special conciliation proposal," which has certain binding force on financial service providers, does not have the same binding force as arbitral award. Arbitration is not included in the financial ADR system. The Arbitration Act is not applicable to financial ADR. However, in view of the de facto binding force of the "special conciliation proposal" in financial ADR, it will not necessarily be pointless to examine whether the provisions of Article 36 of the Arbitration Act concerning the standards of judgment for the arbitration award, which affords the legally binding force, should be construed to be applicable *by analogy* to financial ADR.

One will think that the parties may decide whether to accept the "special conciliation proposal" after reviewing the contents of such proposal, and may consider that it will therefore be unnecessary to examine precisely the standards of judgment for preparing and proposing a "special conciliation proposal." However, in light of such purposes of the financial ADR system as have led to its establishment, as discussed in Section (V)(A) and (B) above, the financial ADR system will not function as intended if the special conciliation proposals are rejected in favor of court decisions. The "special conciliation proposal" should embody the manner of conduct of financial service providers as they ought to be, and is expected to resolve disputes in a manner that is not only acceptable to both customers and financial service providers but also capable of receiving support of the regulators and the public. Insofar as a "special conciliation proposal" has the contents set out above, the financial

[121] Arbitration Act, *supra* note 2.

[122] *Id.* art. 36.

[123] *Id.* art. 45-2.

ADR system requires that it should be accepted by financial service providers. Therefore, for the purpose of examining the standards of judgment for dispute resolution in financial ADR, it would not be appropriate to take it material that the financial ADR system leaves an opportunity for trial of court.

Although the "special conciliation proposal" should have such de facto binding force on both parties, its legally binding force is considerably limited. When the "special conciliation proposal" is presented, financial service providers are obliged by law to accept the proposal except that they can escape from the obligation by, among others, promptly filing suit with respect to the same claim in dispute (in case of the FIEA, financial service providers shall not be obligated to accept the "special conciliation proposal" in any of the cases provided in number 1 to 4 of Article 156-44, Paragraph 6).[124] Apart from the customer's freedom to refuse it, the "special conciliation proposal" is subject to refusal of the financial service provider solely at its will. Both parties may reject a "special conciliation proposal" and instead seek a judgment by the court. Because of this structure, the "special conciliation proposal" is materially different from the arbitral award legally. For these reasons it will be reasonable to conclude that Article 36 of the Arbitration Act shall not be applicable *by analogy* to the "special conciliation proposal."

The "special conciliation proposal" in financial ADR is expected to have similar function in practice as arbitration awards, although materially different from a legal point of view. In view of its possible similarity in practice, it would be reasonable to keep in mind and refer to the standards of judgment provided in Article 36 of the Arbitration Act, in the course of examination of the standards of judgment for dispute resolution in financial ADR.

What does Article 36 of the Arbitration Act suggest in the examination of standards of judgment in financial ADR? Article 36, Paragraphs 1 and 2 of the Arbitration Act require to the effect that arbitral awards shall be determined in accordance with the governing law as provided by the provisions of these Paragraphs.[125] Paragraph 3 of Article 36 requires the parties' "express request" to permit the arbitrators to decide the case according to the principle of "fairness and good (*ex aequo et bono*)" notwithstanding the provisions of Paragraphs 1 and 2.[126] The Financial ADR system imposes on financial service providers the obligation to accept the procedures of the respective designated dispute resolution institutions unless there are legitimate grounds not to do so.[127] When a customer has filed a petition for financial ADR against a financial service provider and the financial service provider has accepted the procedures at the relevant designated dispute resolution institution in compliance with the foregoing obligation, an agreement exists between the parties for resolving the dispute by financial ADR. However, this agreement is not an agreement on the judgment by the principle of "fairness and good (*ex aequo et bono*)" as

[124] Financial Instruments and Exchange Act, *supra* note 6, art. 156-44.

[125] Arbitration Act, *supra* note 2, art. 36.

[126] *Id.*

[127] Financial Instruments and Exchange Act, *supra* note 6, art. 156-44.

required by Paragraph 3 of Article 36 of the Arbitration Act. Accordingly, if Article 36 of the Arbitration Act were applicable *by analogy* to the "special conciliation proposal," it would result that dispute resolution in financial ADR should be made "in accordance with the law applicable to the dispute," but Article 36 would not permit the principle of "fairness and good (*ex aequo et bono*)" to be employed as the standard of judgment, departing from the result of application of law to the dispute. Article 36 of the Arbitration Act suggests that some statutory provisions should be required to permit employment of the principle of "fairness and good (*ex aequo et bono*)" or other similar standard as the standard of judgment for financial ADR.

Article 45, Paragraph 2, Item 9[128]

Article 45, Paragraph 2 of the Arbitration Act stipulates the grounds for refusing to recognize arbitral awards. Recognition and enforcement of arbitral awards can be rejected by the court only in those cases listed in Paragraph 2 of such Article.[129] The list of negative standards of judgment provides a series of material defects which could exist in arbitral awards, and while said Paragraph 2 is not applicable *by analogy* to the standards of judgment in financial ADR, it gives us a useful guidance for the standards of judgment in financial ADR.

Among the cases listed in Paragraph 2 of such Article, Item 9 provides for the case where "the content of the arbitral award would be contrary to the public order or good morals of Japan." As discussed in Section (III)(B)(3) Article 45, Paragraph 2 (Grounds for refusing to recognize an arbitral award) above, dispute resolution by an arbitral award shall not be considered as dispute resolution by law, only when the arbitral award is contrary to the public order or good morals of Japan. In general such arbitral award means, in other words, one which is in violation of mandatory provisions, and one which does not violate mandatory provisions is not such arbitral award.

The judgment for the "special conciliation proposal" can obviously not be contrary to the public order or good morals of Japan or in violation of mandatory provisions, which articulates the limit of discretion in judgment for the arbitral award as discussed above. With a less powerful legal binding force over the disputing parties as compared with that of the arbitration award, the scope of discretion in judgment for the "special conciliation proposal" could, subject to the same limit of discretion as that in judgment for the arbitral award, be broader than that for the arbitral award. This will permit adjudicators to depart from a result of application of statutory provisions (other than mandatory statutory provisions) or judicial precedents for the purpose of implementing the purposes of the financial ADR, as discussed in this article.

[128] Arbitration Act, *supra* note 2, art. 45-2-9

[129] Arbitration Act, *supra* note 2, art. 45.

5. The Basic Principles of Modern Law

The discussions concerning the standards of judgment for ADR in general under "the rule of law" in Section (III)(D) above are applicable to the standards of judgment in financial ADR of Japan. The alternative dispute resolution system is recognized as a part of the judicial system to function in conjunction with the court system and within the framework of basic principles of modern Japanese law. The standards for judgment in financial ADR should be allowed to be flexible, recognizing even soft law as one of their sources of law as stated in the following section (6), but they must satisfy these basic principles of modern law.

6. Soft Law and Code of Conduct (Customary Law)

Among the standards of judgment by ADR practitioners, guidelines of ADR institutions and associations of ADR practitioners and other soft laws, which do not constitute national law, seem to play an important role in practice as customary law, in making decisions regarding the procedures. This is because alternative dispute resolution has a wide variety of cases, both in terms of their content of disputes and with respect to manner and procedure taken for resolution of disputes.

Japanese ADR institutions involved in developing soft laws for ADR in general include the JCAA and the Japan Shipping Exchange, Inc., ADR bodies of bar associations, and private ADR institutions certified by the Minister of Justice.

Rules of designated dispute resolution institutions are important in the development of soft laws for the financial ADR system. To include guidelines of those institutions conducting financial ADR in the subjects to be examined in searching for sources of laws for standards of judgment for financial ADR may look like a tautology, but it is important to understand that the discipline created by general agreement of these ADR institutions does develop soft law.

The code of conduct applied in the financial service industry is also an important source of law.

Among various rules of designated dispute resolution institutions, provisions concerning the standards of judgment for dispute resolution are found in their "Business Operation Rules Concerning Complaint Handling Process and Dispute Resolution Procedure" and the "Detailed Regulations under the said Rules." To determine the standards of judgment, these Rules and Regulations will require to take into consideration the following: (1) agreement (and general terms of contract) with the relevant customer, (2) laws and regulations, such as civil law, and those regulating the relevant financial service industry, (3) regulators' supervisory regulations, including supervisory guidelines and inspection manual, and (4) code of conduct and business operation regulations set by associations of financial service providers. The above Rules and Regulations will also prescribe the procedures necessary to be taken at each of the phases from application stage to the end of the procedures, and the number of days required for the procedures.

All these guidelines, various rules and code of conduct constitute a part of the sources of law to determine the standards of judgment for financial ADR, but their legally binding power or validity is subject to higher ranking sources of law. For instance, the validity of any of their provisions which provide for limitation of liability of financial service providers may be limited or denied by national laws or regulations.

7. Precedents in Financial ADR

Precedents of financial ADR will accumulate in coming years. The purposes of financial ADR is to maintain the public trust in the financial system by presenting a code of conduct to financial service providers and requiring their compliance with such code as well as providing appropriate resolution of individual disputes. Thus, the content of individual cases and the resolution provided by designated dispute resolution institutions are, even if names of individual disputing parties are not publicized, expected to play an important role as precedents.

The accumulation of precedents in financial ADR will provide financial service providers, dispute resolution providers, as well as the people with practical guidelines with respect to the standards of judgment in financial ADR. These guidelines will, with the approval of the court, develop to code of conduct and become law.

8. The Meaning of the "Fair and Reasonable (*Jori*)" Test

In the foregoing discussions of the sources of law for the standards of judgment in financial ADR, we have seen some phrases in the statutory provisions indicating the standards of judgment. They are "it is considered as suitable in light of the nature of case, the parties' intention, the parties' conduct in the procedures, and any other circumstances;"[130] procedures "shall be executed in a fair and appropriate manner" and dispute resolution shall be "based on specialized expertise" and "properly responding to the actual conditions of the dispute;"[131] and to aim "at finding such a resolution as is "fair and reasonable and is suitable in properly responding to the actual conditions of the case" and to make a decision after "taking the equity of both parties into consideration."[132] As stated so far, these phrases intend to mean "satisfy[ing] the fair and reasonable (*Jori*)" test and the "fair and reasonable (*Jori*)" test means "common sense" prevailing in the society and, in financial ADR, it can be expressed as "good sense" in the relevant financial service industry.

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[130] Financial Instruments and Exchange Act, *supra* note 6.

[131] ADR Promotion Act, *supra* note 8.

[132] Civil Conciliation Act, *supra* note 1.

"Fair and reasonable (*Jori*)" is a term used in Article 1 of the Civil Conciliation Act.[133] Meaning of this term, as a part of that statute and a term expressing the standards of judgment in financial ADR, should be clarified by interpretation through individual financial disputes. If we try to clarify its meaning in general, we will only be able to paraphrase it into "common sense" or "good sense" as stated above.

In jurisprudence, the Japanese language term "*Jori*" is sometimes used to signify the natural law, which serves as ground of the positive law, or to mean the interpretative standards which should lead interpretation of law to fill gaps in the law. It should further be noted that, in the hierarchy of sources of law for their application, it comes after written law, customary law, and court decisions when "*Jori*" is acknowledged as a source of law. Such a variety of meaning of the term "*Jori*," as used in jurisprudence, could be highly suggestive in searching its meaning when the same term is used in the positive law.

E. Guiding Principles for Determining the Standards of Judgment

Taking into consideration together the purpose and unique features of financial ADR and the accomplishments of the standards of judgment in financial ADR required by disputing parties and others, as discussed in Section (V)(A), (B), and (C) above, I would now like to analyze those requirements which adjudicators should bear in mind in making their judgments according to the sources of law in (D) above. Their judgments are not limited to those concerning development of the content of a settlement proposal. Adjudicators are also required to make judgments concerning the procedures, such as what procedures should be taken for finding the facts, or whether a disputing party's request for examination of evidence or cross-examination should be accepted or refused, and these judgments will affect easiness, flexibility and promptness of dispute resolution. The requirements will be analyzed with a particular focus on such needs for handling customer complaints against financial service providers and for providing resolution of disputes with customers as have led to the establishment of the Financial ADR system.

The requirements set forth below can be listed as guiding principles for establishing the standards of judgment. An adjudicator is required to examine all of them and verify that all of them are satisfied by the judgment he is about to make.

(1) It presents a flexible solution in accordance with good sense.
(2) It serves, through customer protection, for maintaining and enhancing customers' trust in financial service providers.
(3) Its content serves for seeking ideal financial services and the code of conduct of employees of financial service

[133] *Id.* art. 1.

providers and contributes to their improvement and establishment.

(4) It is a procedure which is not burdensome to customers.

(5) It aims at a flexible procedure free from the procedural requirements of litigations.

(6) It provides a prompt and efficient dispute resolution procedure, from filing of a complaint against financial service providers to the presentation of a proposal to resolve the dispute.

(7) Its content and the reasons for the judgment can be communicated clearly not only to the disputing parties but also to financial service providers in general and the people so that they can evaluate and criticize them.

(8) It strongly requires both parties be candid and honest, and imposes strict sanctions against false allegations.

Among these, the requirements in (2), (3), and (7) above will show characteristics of the standards of judgment for dispute resolution in financial ADR in comparison to the standards of judgment for ADR in general.

I would like to add some supplementary explanation with respect to the requirement in (8) above. If both the financial service provider and customer involved in the dispute are honest and candid, no conflict would occur over the facts themselves, although there could be different points of view, and different ways of understanding, of one and the same fact. If there is no conflict over the facts, it will no longer be necessary to hold a hearing to examine witnesses or hear from the parties, making the whole financial ADR procedure concise and prompt without the parties' objections. Therefore, in financial ADR, it is extremely important to make the parties honest and candid. To that end, it is important that financial service providers, at first, require their employees to be honest and candid. For financial service providers, the financial ADR system should be considered as a system which not only provides an opportunity for defense against claims and disputes but also gives a chance to find a problem in their employees and to retrain them. Customers should also be required to be honest and candid. It is important for adjudicators to exercise their ingenuity in finding the facts and to take a strict attitude against false allegations.

F. Summary

The efforts to clarify the standards of judgment for dispute resolution in financial ADR seems to come down to the conclusion that judgment should be made in accordance with the "fair and reasonable (Jori)" test and in compliance with the purpose of the financial ADR system. The "fair and reasonable (Jori)" test can be understood to mean "common sense" prevailing in the society or "good sense" in the relevant financial service industry. To make judgment in compliance with the purpose of the financial ADR system means that judgment concerning a dispute related to the financial service

industry should be made with a view to accomplishing the purpose of the financial ADR system, that is "recognizing the public nature of the financial service industries, not only to ensure sound and appropriate operations of the business but also to aim at protection of customers to maintain credibility of financial service industries in the people's mind."

If a judgment is made in compliance with these purposes and insofar as it is made in accordance with "good sense," it can depart from, and is not bound by, a result of application of statutory laws or court precedents.

Such judgment will be required to be made flexibly, in accordance with good sense, and in light of the code of conduct which shall be abided by in providing financial services to customers and the benefits which financial services should provide to customers, and with the benefit of adjudicators' consistent efforts to understand the role of financial system in the economy and society, and with the advantage of their expertise knowledge of the contents and mechanics of financial products and financial services and the actual manner of business prevalent in the industry. Such judgment, if made as aforesaid, should contribute to sound and appropriate development of the financial system and should result in protection of customers.

In financial ADR, adjudicators should by themselves seek a desirable code of practice for financial service providers and their employees. Such a code of practice is also expected to become more sophisticated and precise through the accumulation of actual cases of dispute resolution in financial ADR. Thus, financial ADR will contribute to the development of law in the financial field. The standards of judgment for dispute resolution in financial ADR must be such that will result in "flexible judgments in accordance with good sense" which can be made by application of such a code of practice.

VI. CHECKLISTS FOR JUDGMENT AND THE FUTURE CHALLENGES

Taking into consideration the foregoing discussions in "III. The Standards of Judgment for ADR in General" and "V. The Standards of Judgment for Dispute Resolution in Financial ADR of Japan," I would like to examine and enumerate some elements which the standards of judgment for financial ADR must be equipped with. These elements will be composed of those which will be found by examining the requirements in Article 3, Paragraph 1 of the ADR Promotion Act[134] providing for the basic principle of alternative dispute resolution procedure, Article 1 and 17 of the Civil Conciliation Act,[135] the requirements of "the rule of law" and "due process" for protection of rights, and those elements listed in "Guiding Principles for Determining the Standards of Judgment" in Section (V)(E) above.

[134] ADR Promotion Act, *supra* note 8, art. 3.

[135] Civil Conciliation Act, *supra* note 1, arts. 1, 17.

A. Positive List of the Standards (Positive Requirements)

A judgment for dispute resolution in financial ADR must satisfy all the following requirements:

(1) It respects the parties' voluntary efforts to resolve their dispute.
(2) It is made after taking fair and appropriate procedures.
(3) It reflects expertise knowledge of finance.
(4) It aims at resolution of dispute in a manner appropriately corresponding to the actual conditions of the dispute.
(5) It aims at prompt resolution of disputes.
(6) It presents a proposal which will resolve the dispute flexibly and in accordance with good sense.
(7) It can be evaluated as aiming at dispute resolution by law. To put it in detail, it satisfies either (a) or (b) of the following:
    (a) It is consistent with a result of application of law to the case.
    (b) When, after having considered applicable law, a settlement proposal or a special conciliation proposal is prepared with contents which depart from a result of application of law;
        (i) it has been determined that such a result shall not be suitable in light of all the circumstances of the case, with a clear determination as to the extent by which the judgment considered as suitable differs from the result of application of law and the reasons why the difference is considered appropriate, and
        (ii) although it is different from a result of application of law which is directly applicable to the dispute, it is consistent with the judgment which is considered appropriate by application of the "fair and reasonable (*fori*)" test, "good sense," or "equity and good" when the following (8), (9), and (10) are taken into account.
(8) It is consistent with applicable regulator's supervisory criteria, such as supervisory guideline and inspection manual, and applicable code of conduct and code of business operations established by the relevant industry association.
(9) It contributes to the establishment of such financial service and such code of conduct of employees of financial service providers as have been acknowledged by the adjudicator ideal after his or her pursuit thereof.
(10) It is useful for maintaining and enhancing customers' trust in financial service providers through the protection of customers.
(11) It aims at a procedure which is not burdensome to consumers.
(12) It aims at a flexible procedure free from procedural requirements in litigations.
(13) It offers a prompt and efficient dispute resolution procedure, from the filing of complaint against financial service providers

to the proposal of solution.

(14) The judgment and reason thereof can be communicated clearly not only to the disputing parties but also to financial service providers in general and the people so that they can evaluate and criticize them.

(15) It is a judgment that urges the disputing parties to take candid and honest attitude in alleging facts in financial ADR and, with respect to the particular dispute before the adjudicator, is a judgment made after having reached the situation where remaining facts in dispute are only those which should still remain in dispute even if the both parties have acted candidly and honestly.

B. Negative List of the Standards (Negative Requirements)

In the sources of law for the standards of judgment in financial ADR as discussed in Section (V)(D) above, I would like to identify those matters which a judgment should not fall under; in particular from the business of the designated dispute resolution institutions stipulated in the FIEA or other laws regulating the financial service industry (in case of FIEA, Article 156-44, Paragraph 2, Items 4 and 5)[136] and from Article 14 of the Civil Conciliation Act, which would taken into consideration in financial ADR,[137] and with reference to Article 45, Paragraph 2 of the Arbitration Act,[138] which should be referred to due to the de facto binding force of the "special conciliation proposal."

A judgment for dispute resolution in financial ADR must not fall under any of the following:

(1) The settlement proposal or special conciliation proposal is not considered necessary for the resolution of disputes related to the financial products handling business or any other financial service business.

(2) Content of the settlement proposal or special conciliation proposal exceeds the scope of the requested relief.

(3) The disputing parties did not receive proper notice necessary for making their allegations and submitting evidence, or were not given the time necessary to do so.

(4) The procedures were not conducted fairly and appropriately.

(5) Content of the settlement proposal or special conciliation proposal will jeopardize the public trust in the financial service industry, or is otherwise not suitable in light of the purposes of financial ADR. This would include the case where a party who is

[136] Financial Instruments and Exchange Act, *supra* note 6, art. 156-44.

[137] Civil Conciliation Act, *supra* note 1, art. 14.

[138] Arbitration Act, *supra* note 2, art. 45.

not candid or honest receives benefits.

(6) Its contents are contrary to the public order or good morals of Japan.

As stated in (6) of the positive list in Section (VI)(A) above, a settlement proposal or "special conciliation proposal" in financial ADR is required to present a proposal which will resolve the dispute flexibly and in accordance with good sense. Therefore, in applying (2) of the above negative list, it is necessary to pay attention to ensure that such a flexible resolution proposal will not be considered to fall under (2).

Presentation of the positive list (positive requirements) and negative list (negative requirements) is an attempt to start their development. From this starting point, it is expected that a checklist useful to employees of designated dispute institutions and adjudicators will be developed through accumulating practice of financial ADR and by exchange of experiences of designated financial dispute institutions. As practice of financial ADR accumulates, it is expected that many items in the checklist will no longer necessary to be specifically listed as they become common sense in financial ADR. When it does happen, the checklist will become more concise.

C. Presentation of Issues for Future Consideration

On November 28, 2008, the Japan Financial ADR/Ombudsman Research Group announced a proposal with respect to a desirable financial ADR system, under the title of "A Model for a Financial ADR Organization and Measures for Its Realization — Toward the Development of an Effective and Reliable Financial ADR System for Reasonable and Flexible Dispute Resolution" (hereafter referred to as the "Research Group Proposal").[139] The Research Group Proposal stated that the ideal financial ADR organization is required to satisfy, in respect of its resolution of financial service disputes, the following eight basic requirements (constituting the eight principal design concepts for the organization): flexibility, promptness, simplicity, assured expertise and quality, ease of access, comprehensiveness (across the financial service industries) and fairness (including independence and transparency), and confidentiality. These eight requirements must, therefore, be satisfied in designing the organization and in its operation of business.

Japan's financial ADR system was established in 2010 with a view to satisfying all these principal design concepts, except for "comprehensiveness," while its purposes are yet to be fulfilled. While the financial ADR system will have to cope with its difficulty in providing easy access to customers due to its

[139] Teigensho (shohan dai nisatsu) (提言書 (初版第 2 刷)) [*Japan Financial ADR Ombudsman Study Group Proposal (Original Version, 2nd Printing)*], Kinyū ADR Onbuzuman Kenkyūkai (金融 ADR オンブズマン研究会) [JAPAN FINANCIAL ADR OMBUDSMAN STUDY GROUP] (Dec. 8, 2008), http://www.kinyu-adr.jp/Top/News/teigenshoshohandai2satsunokoukai.

failure to satisfy the "comprehensiveness" criterion and will have some other challenges for its future development, it has now been given the present framework and commenced its operations.

Facing complaints and disputes in individual cases, employees of designated dispute resolution institutions and adjudicators will make judgment on a case-by-case basis relying on their expertise. In order to enable the judgments for dispute resolution in financial ADR to satisfy the purposes of the financial ADR system and to enable the financial ADR system to show, by presenting clearer standards of judgment, the rules of conduct to financial service providers and the public, there could be raised certain issues which should be examined in the future. These issues are set forth below.

1. Challenges of Designated Dispute Resolution Institutions

I would like to enumerate important issues which should be tackled immediately by every designated dispute resolution institution.

(1) Improve customer (consumer) evaluation of the financial ADR.
(2) For this purpose, make the complaint receiving and handling procedures consumer friendly first.
(3) Examine the standards of judgment, reexamine customer handling policies, and provide thorough training within the dispute resolution institution.
(4) Facilitate information exchange with financial service providers who are members of the dispute resolution institution, and enhance cooperation with member financial service providers' complaint handling and dispute resolution procedures and other processes.
(5) Strive for creation and reexamination of code of conduct or standard of industry practice, in cooperation with financial service providers.
(6) Continuously examine the standards of judgment and continue research and training within the dispute resolution institution so as to make it possible to provide, in individual cases, equitable and appropriate judgments in a stable and prompt manner (It is especially important to establish and maintain a clear guideline on the attitude and procedures for the designated dispute resolution institution and their adjudicators in dealing with any potential dispute over facts.)
(7) Strive for collaboration with other designated dispute resolution institutions.

2. Challenges of Financial Service Providers

Designated dispute resolution institutions depend on their member financial service providers for financial resources. In order to enable

designated dispute resolution institutions to tackle the challenges described in (1) above and to achieve their goals, financial service providers will have to address the following challenges:

(1) Increase transparency of their designated dispute resolution institutions' business.
(2) Increase the number of full-time workers engaged in financial ADR.
(3) Increase funding to their designated dispute resolution institutions for increasing the number of full-time workers.

It is obvious that we need considerable human and physical resources, and for efficiency concerns, it would be necessary to create by consolidation a single designated dispute resolution institution across the financial service industry. These challenges are left mainly to the judgment of financial service providers rather than to officers, employees, or adjudicators of designated dispute resolution institutions.

3. Challenges of the Government

I would like to raise some issues which must be examined by the Diet, administrative bodies, and the courts.

Stipulation of the standards of judgment

It is desirable to expressly stipulate in a statute an outline of the authority and scope of discretion of the adjudicators in financial ADR. This legislation will clarify the authority and scope of discretion of designated dispute resolution institutions and their adjudicators and will activate the financial ADR.

Review of the obligation of confidentiality

In the present financial ADR system, adjudicators, officers, and employees of designated dispute resolution institutions, and those who used to have such positions, shall not divulge any confidential information which they have learned during the course of their duties (Article 156-41 of FIEA and other comparable provisions in other financial service industry laws).[140] The obligation of confidentiality as such is the one which a dispute resolution provider shall generally have in alternative dispute resolution conducted in the private sector. It is considered as one of the characteristics and advantages of ADR, in contrast to the public trial. The obligation of confidentiality in financial ADR has been introduced following the introduction of the same obligation in general ADR.

However, the financial ADR does not just provide relief for individual consumers but also undertake a role of developing the infrastructure of the financial system, with its goal to maintain the public's trust in the financial system. To achieve this goal, a "special conciliation proposal" must be disclosed with the content of the case, and the accumulation of such proposals must become not only the information available for the regulator's supervisory administration of financial service providers but also the information to indicate the industrial order which the financial ADR presents to the people and financial service providers. In addition, in order to make financial ADR an alternative dispute resolution satisfying the requirement of the rule of law, financial ADR must provide information to make its result predictable to the people and financial service providers. Furthermore, a "special conciliation proposal" must be disclosed in courts, together with the content of the case, in order to make the financial ADR a dispute resolution procedure which functions in collaboration with court proceedings, as stated in the next section regarding collaboration with court proceedings.

Financial ADR must be made free from the obligation of confidentiality to the extent practicable to satisfy these requirements.

Collaboration with the court proceedings

Suppose a special conciliation proposal was not accepted and a lawsuit was brought for the same claim in the subject dispute, how will a court handle the adjudicator's judgment by which he prepared the "special conciliation

[140] Financial Instruments and Exchange Act, *supra* note 6, art. 156-41.

proposal" and presented to the parties with reasons? If there is no institutional collaboration between the financial ADR and the court, the financial ADR system will theoretically be an inefficient dispute resolution system from the perspective of social cost.

This raises the issue that it would be necessary to provide an express statutory provision to clarify the legal authority of financial ADR judgments in the judicial system. If courts do not have the authority to carry forward judicial procedures based on the procedures taken by financial ADR, the financial ADR system cannot reduce the social burden for financial dispute resolution, and in addition becomes a weak dispute resolution system solely dependent upon the agreement of disputing parties. The financial ADR system must be recognized as a part of the judicial system, and hold a position in the judicial system with a clear relationship with the court. For that purpose, we need a system where an outline of the standards of judgment for dispute resolution in financial ADR is defined by a statute, and the content of such standards is clarified through interpretation by the court. In order to establish financial ADR as an ADR system with administrative purposes, it is necessary to clarify its administrative purposes and its position within the judicial system. Judgments in financial ADR and judgments in court should together present to financial service providers and customers concrete rules which are applied in financial ADR. Otherwise, the financial ADR system cannot be considered as a system which satisfies the requirement of "the rule of law" for providing clarity and predictability of rules.

In the UK's financial ADR system, these issues have been clarified and resolved by the 2000 FSMA[141] establishing FOS, and the FOS Rules and Guidelines under that Act. Courts unambiguously interpreted these laws and rules, and also made clear the role and the future direction of FOS. Furthermore, courts clarified the financial ADR system's position in the legal system and expressed their expectations of its future development.

4. Closing Remarks

How can we tackle these issues concerning financial ADR in Japan? Will financial service providers appreciate the value of the financial ADR system and take steps to meet their challenges discussed in Subsection 2 above? Do we resolve these issues raised herein by legislation? What could be done under the present law by the supervising regulator of the financial service industry or the administrative agency responsible for consumer protection administration? Will the court clarify their policy about how to handle the "special conciliation proposal" presented in financial ADR? The financial ADR system was established with these challenges. It is dependent on the expertise of employees and adjudicators of designated dispute resolution institutions and others engaged in the financial ADR.

[141] FINANCIAL SERVICES AND MARKETS ACT, *supra* note 3, c. 8, §§ 225, 228, 229.