Outside Currents Strike a "Small Island Nation": Global Trade and Japan's Contractual Flexibilities

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INTRODUCTION

Any North American architect observing Japanese design development cannot help but wonder at the ability of Japanese architects to negotiate the quality and execution of design after a project has been bid and contracts negotiated. I have seen site surveys done at the onset of construction, after the project has been bid. Suppliers and quality of building components found in later stages of construction (windows, doors, etc.) are determined shortly before installation. Contracts often remain unsigned through basic design, until well after the engineer's calculations and such have been completed – and one author notes a case where a contractor had demolished an existing building and begun advertising units for sale in a new building prior to contracts being signed on the project.

The basic assumptions found in legal systems in the United States and Japan are diametrically different, with the practices of most other developed nations standing somewhere between the two. In the U.S., contracts are considered to tightly define the relationship and responsibilities of each party, without regard for the fairness or appropriateness of the agreement. Therefore, U.S. courts will strictly enforce a contract. But, as the legal scholar Hiroshi Oda noted, Japanese courts have decided that contracts should be reviewed, "taking into account the doctrine of good faith and fair dealing..." More significantly, as another leading scholar noted, "in case after case... the courts continued to refuse to enforce contracts according to their explicit terms." As a result, in Japan contracts are generally perceived as being inexact, adaptable instruments.

THE JAPANESE CONTRACT

The Japanese doctrine is that, as Oda states, "contracts concluded where one party is in a strong bargaining position and which contain excessively disadvantageous clauses as regards the other can be null and void..." In the United States, by contrast, the courts will enforce a morally tainted contract (the common example is trading one's inheritance for a bowl of soup) on the assumption that both parties felt it a worthwhile bargain at the time of execution. Thus the foundation of the Japanese contractual relationship encourages vaguely written contracts. Japanese legal scholars are unequivocal on this point: Eiichi Hoshino notes that "the general notion of the binding power of contracts is weak in Japan" and that <quote>"... the precise drafting of a contract itself is not very desirable." And Oda claims that 'the binding force of contract is not as strict as in Europe and the United States.' One can say, in a word, that in Japan little interest is paid to what are called contracts."

Contracting parties do not pay much attention to the content of contracts, and may even work with no more than an oral agreement. In 1979, the Ministry of Construction found that over one quarter of all construction contracts were no more than a simple written order and its acknowledged acceptance. About 80 per cent of general contractors surveyed normally completed a contract with owners, with an additional twelve per cent using only a written order and/or its acceptance, and slightly more than five per cent undertaking work on the basis of an oral contract. Subcontractors or architects also enter into projects with little more than a verbal agreement, further eroding those claims to tailoring their legal rights which Westerners consider necessary. Practices between subcontractors and the general contractor were particularly loose, with only 39 per cent utilizing contracts, and nine per cent relying only on an oral agreement, although the Construction Business Act requires a written contract. (The reasons that a contractor is more likely to require a contract when working with an client, and less concerned about binding legal documents with subcontractors is a point I will further address below.) Manufacturers, too, offer testing, prototype development, and other services for free and without contracts.

One reason that it may be beneficial to draft contracts without extensive clauses (which Western academics have referred to as "incomplete contracts") is that it is often quite costly to develop an agreement which covers all possible occurrences – and even then, as many architects are aware, the interpretation of these clauses on each side may differ, leading to problems. Bob Greenstreet, in a discussion of suits

against architects, goes so far as to note that, "Many of the cases ...often result not from design failure...but from a breakdown in the contractual relationship, due to misunderstandings, miscommunications, or a general lack of comprehension." It is conventional in many countries for architects, prior to commencing construction, to produce extremely detailed construction documents as part of the contract, but in spite of this, not all aspects of the building can be adequately addressed in such documents. In addition, changes in material prices and availability or less than ideal conditions on site may require change orders. But Greenstreet notes that "...the change order process is a fertile area for the inception and growth of disputes." As a result, one legal text on construction practices in North America notes grimly that, "Construction is a dispute-prone industry, and claims are a fact of life. Even successful projects have claims. Claims are a natural outgrowth of a complex and highly competitive process during which the unexpected often happens."

Instead of a detailed agreement, Japanese contracts simply call for unforeseen events to be addressed in a cooperative spirit. The idea is that the use lack of contracts not only encourages mutual trust in the relationship, but allows for adaptability in unforeseen circumstances. In a lengthy essay on contracts, Takeyoshi Kawashima notes that the contractors advising the national government have even preferred this approach. He wrote,

> "On one occasion I suggested that the contents of the standard provisions of the construction work contract of the Ministry of Construction be made as complete, inclusive, and definite as possible. This was because I thought that it was, above all, necessary to narrow the margin for deciding disputes between the contracting agency and the contractor through negotiation...There was opposition to my proposal from the business world [e.g., contractors]...If the obligations under the contract were made definite and fixed, it was said, an uneasiness was felt that such contracts would 'lack flexibility'."

Because of this tendency towards versatility, agreements are frequently drawn up without the involvement of legal counsel. Yoshinobu Ashihara has even been quoted as saying he will not accept projects when the client uses a lawyer in negotiations. And Tadao Ando reflected the Japanese attitude toward the involvement of lawyers, noting, "If in Japan you came to a meeting and said 'this is my lawyer,' the person you were meeting would get upset. But in America, you have the feeling that people say 'that's right. I don't trust you.'" Regarding this approach, Fumihiko Maki said, "In Japan, we are still able to change design in construction without too much litigation...We have taken advantage of this. The final product is a collaboration."

CONTRACTS IN JAPAN'S LEGAL AND SOCIAL COMMUNITY

Two scholars who have studied legal practices in the United States and Japan, Minoru Nakazato and J. Mark Ramseyer, refer to the U.S. approach to contracts as a negotiated "private legal regime" and many scholars consider the U.S. approach to be overly "legalistic." Most further suggest that the Japanese legal context allows for simpler contracts because there is little occasion for privately negotiated variations and thus not only is there less need for highly specific documents, there is little opportunity to utilize them. Generally speaking, the Japanese courts will not simply consider a specific contract, but also look to industry norms and to practices which already existed between contracting parties. The Japanese courts have noted that custom has greater weight than the language found in contractual agreements – the precise opposite of what one would find in U.S. courts. For example, the Tokyo District Court has dismissed detailed boilerplate in a lease as no more than "a model" and "not intended by the parties to have any effect." This attitude is also found outside the courts. In a 1971 and 1976 set of surveys by the Nippon Bunka Kaigi [Japan Culture Forum] the questions included "What would you do if a contract became unsuited to the actual situation a few years after it was made?" While slightly more than 31 percent of respondents agreed to the answer "However unsuitable, a contract is a contract and I would abide by it," over 60 percent of all respondents selected the answer "I would discuss with the other party whether the contract could be ignored." Notably, the survey did not even offer an answer regarding renegotiating a contract or writing a new one.

One point that many scholars writing on Japan's legal system tend to regard as central to the flexibility of contracts is the impact of "changed circumstances." In both the United States and Japan, it is possible for one to be excused from carrying out contractual obligations if there have been unforeseen changes which make complying impossible – U.S. scholars, for example, tend to discuss the impact a war has on shipping supplies. And in fact it was circumstances surrounding World War II which led the Japanese Supreme Court to decide that a contract is no longer binding if the context under which it was written has changed. Broadly speaking, the definition of changed circumstances is similar in the United States and Japan. In the United States, a contract may become moot when its purpose expires, e.g., when an architect hired for particular expertise dies before being able to complete a project.

Additionally, changed circumstances may make it physically or commercially impossible to complete a contract, for example when an earthquake makes a building site unsound. These points are usually outlined in three conditions under which a U.S. contract becomes untenable: first, the change in circumstances must not have been foreseen; second, the party attempting to nullify the contract must not have directly or indirectly accepted the risk associated with the change; thirdly, the party seeking to nullify the contract must

not have been responsible for the changed conditions. However, one notable difference between the two systems is the potential scope under which these changes are considered.

In Japan, the conditions that can lead to a contract becoming invalid are broader, and by coincidence more closely relate to the practice of architecture. In fact, the issue of changed circumstances takes up a considerable amount of space in the relatively short standard contracts used by most architects and contractors. Fumio Matsushita includes such standard contract forms in his book, *Design and Construction Practice in Japan;* these permit the parties to demand renegotiation if one year has passed and if "...the contract price has become inappropriate due to changed wages or commodity prices..." or due to "...drastic changes in the economic conditions..."

Although contractors have attempted to limit the cost of fluctuations during the 1990s (because they create economic uncertainty), an earlier survey demonstrates the use of this clause. In the early 1970s, the combination of a shift from the gold standard in the United States and rising oil prices created a rapid drop in Japan's economy. At that time, the Tokyo Chamber of Commerce and Industry surveyed its 300 member firms regarding exploitation of the "changed circumstances" clause in construction projects. Two-thirds of all firms attempted to exploit this clause, and one half did so successfully, with larger firms generally more fortunate. Thus, normal practices are such that architects and contractors treat contract documents, which are often ambiguous in any case, as pliable – especially as they relate to price and deadlines.

CONTRACTS IN JAPAN'S ARCHITECTURAL COMMUNITY

One leading Japanese legal scholar claims that "even if detailed provisions are inserted into contracts, they do not have very much significance; and consequently, the parties do not read them carefully or regard them seriously." And Fumio Matsushita, legal counsel for one of Tokyo's largest design offices, noted "...a contract is not finally binding upon the parties, no matter how exactingly bargained and drafted. If one party experiences difficulty in performing, he can and usually does propose a change to the contract and the other party is expected to give certain consideration..." He continued, "In Japan...negotiations do not precede, but follow the conclusion of a contract and continue without end."

As one example of how this prevails in architectural practice, legal deadlines are more flexible. Firm deadlines, particularly the imposition to the minute of bid deadlines on government projects, are a source of amazement and amusement to Japanese architects and contractors who have had experience in the United States. In general, any contractual deadline is only a target. As Kawashima noted in his essay, "The Legal Consciousness of Contract in Japan," "...even something such as the due date of a debt is not thought of as something strictly defined but as fixed 'give or take a few days.' " Kawashima additionally notes that construction contracts tend to offer a great deal of leeway through built-in extensions, and that as long as the other party is not inconvenienced, these extensions should not incur penalties. Furthermore, because the precise scope of work in each phase is more loosely defined, architects and contractors can frequently shift incomplete work to the next stage of production when necessary.

Thus, in one extreme example I studied, Aoki Jun's "Snow Research Lab" was officially completed in December, but remained without an operable air handling system until June – in spite of the fact that the building had been specifically designed and constructed to study the use of stored snow in small-scale cooling systems. Office staff moved into the building in February, but as the mechanical system was incomplete, they relied on space heaters to offer some comfort. I visited the project on the day the air handling systems were first put to use. The client representative and mechanical contractors were on cordial, even friendly, terms.

While the current shift to performance specifications will have a significant impact, today uniform standards generally establish specifics such as tolerances, rather than project-specific contracts. In the case of construction tolerances, I found the agreed upon norms already more precise than would be expected in North America – but I also observed staff from Toyo Ito's office successfully putting pressure on fabricators to work with still tighter tolerances for particularly important parts of Sendai Mediatheque, without any contractual rights to do so.

Contrast this with Western practices, where instead of a measure of a reasonable maximum variation, builders often treat tolerances as the acceptable slack. Since in Japan the emphasis is on the relationship between parties, rather than a legalistic assertion, the fabricators tend to either work harder to meet the architects' stated higher standards, or occasionally, ignore them in such a way as to indicate a reluctance to continue the working relationship. In the later case, as I have discussed elsewhere, other firms generally exist within the building team which are able to take on production. It is more likely that the second firm will receive greater work than originally anticipated, rather than the design team making a dubious attempt to pressure the reluctant fabricator to work at a higher standard. (I should emphasize that the oligopolic structure of Japan's construction industry, with a limited number of large contractors dominating the most profitable construction sectors, means that there is a high cost involved to the fabricator that loses work in this manner.)

Furthermore, if parties in Japan do not specify the quality of a material, the courts have generally mandated intermediate quality. As a result, much of the detail of North American specifications is not initially necessary in Japanese documents, and the documents that exist for the most part resemble outline specifications. Japanese architects may write performance specifications, but these are generally related only to the production of unique or previouslyuntried build-

ing components. Rather than relying on the initial specifications to establish quality, I have noted the use of extremely specific agreements produced during the construction phase. The contractor usually writes these, with modifications suggested by design professionals before document approvals. As one example of such an agreement, on the site of a modest building under construction by Shimizu the contractors had a binder several inches thick, related to unfinished concrete on the project. Topics covered included the quality of the formwork, its thickness, form ties and separators, the composition of the concrete, supplier location and the distance from the plant to the site. In reviewing the document, the architect noted a desire to assure that the nail heads in adjacent panels of the formwork would be aligned, a level of detail beyond the scope of most North American specifications.

While an open-ended legal context allows for the professional to react quickly, detailing and measuring for existing construction, or taking into account changes in the cost and supply when selecting materials, the environment is not one which is entirely positive. First and foremost, loose contracts mean that each project requires a new relationship to be established between the architect and contractor, and the actions possible on one site might, in spite of the architects' best effort, be unavailable on the next. Even where the same contractor is involved, much depends on the inclinations of the individuals representing both sides on site. The ability to negotiate successfully in such relationships is not one that comes easily. Although the best projects exemplify the innovations possible under a flexible legal structure, Japanese architects also recognize the benefit of a tightly defined contract. As one example, I have observed many projects where the budget is redefined by the client during construction, generally (in Japan's current recession) reducing the funds available – in the fiscal year ending in April of 1998, for example, the Japanese government made across-theboard cuts of fifteen per cent to all projects under design or construction. Such shifts mean that architects in Japan must constantly renegotiate areas that many architects consider fixed.

POLITICAL ECONOMISTS' JUSTIFICATION FOR "INCOMPLETE CONTRACTS"

The flexibility of contracts, as I noted above, relates to a strong inclination towards mutual trust. In that regard, Japan's relatively closed community has made such contracts more likely, although there are certainly other environments where similar agreements are possible. Legal scholars suggest that a society's willingness to enforce contracts tightly or not is in part a result of expectations regarding the longevity of business relationships. As Cooter and Ulen note, "Sharp dealing is far more likely when the contractual partners never expect to see each other again than when they have an interest in continuing trade." In game theory, this is referred to as the "End Game Problem." In short-term relationships, the benefit of cooperation is not perceived as being significant, but in ongoing relationships the reverse is true.

In a discussion of similar attitudes towards contracts found in rural communities in the United States, the legal scholars Minoru Nakazato and J. Mark Ramseyer argued:

> "Whether in Japan or the United States, how much firms A and B use and rely on legally enforceable contracts will depend on several often closely related factors:
> - the extent to which A and B are tied to a small, closely knit community
> - the speed and accuracy with which information travels among the firms with which A and B deal.
> - the number of other firms with which A and B do business.
> - the degree to which A and B have invested time and resources in their reputations for integrity.
> - the extent to which A and B can use assets, guarantees, or controlling stock interests to secure their performance.
> - the degree to which, wholly aside from these factors A and B can credibly convince each other that they can rationally expect to continue to do business with each other in the future."

Clearly, the limited number of major contractors, developers, and architects working in Japan make ongoing relationships the norm. Further, most of these factors are far more a part of the landscape of architecture and construction practice in Japan than they are, for example, in the United States. National size and a common language can also contribute to a sense that one is working in a small community – which may explain why some European construction communities also hold a loose attitude towards contracts. But even on this point, Japan's linguistic barriers and regulatory are certainly higher. Thus, many scholars discussing the fabric of legal and business communities note that "The literature on business transactions and contracting in Japan suggest a predominant emphasis on repeated deals based on relationships established over time and avoidance of spot transactions with strangers." Therefore, as long as Japan's construction community remains a relatively closed one, the authority of long-term relationships over specific contracts will probably continue.

CONCLUSION

Over the past ten years, the U.S., goaded by Senator Frank Murkowski, has attempted to force open Japan's construction industry to international trade. Understandably, the differences between Japanese attitudes and Western attitudes towards contracts and agreements is one of the major factors which has contributed to continued failure of U.S.-Japan trade agreements. While to date these efforts have been limited, there has been impact. In its economically weakened state, Japan has been forced to concede to the U.S. on a

number of important issues. As the Japan External Trade Organization acknowledged in a survey on access within the construction market published in 1998, "Japan has made a particular effort to open its markets through deregulation and other measures..."

If U.S. efforts are successful in opening the construction industry, this will impact currently flexible attitudes regarding contracts in Japan's construction and design community, since it changes the context for contracts. Japan's construction would no longer be controlled by a small, closely knit community, information would no longer be as reliable, and – with a much larger number of firms involved – individual corporations would no longer believe that repeat business was likely.

Indeed, even today, the six criteria outlined by Nakazato and Ramseyer no longer accurately describe Japan's construction community. The long recession of the 1990s has weakened one criterion, the extent to which both parties can use assets, guarantees, or controlling stock interests to secure their performance. Assets have eroded to the point that several major contractors would already be bankrupt in many countries. Further, cross-holding shares of stock, a practice which has held together contractors, suppliers, and architectural firms (most Japanese corporations, whether small professional firms offering architectural services, or larger manufacturers, are *kabushiki kaisha* or joint-stock corporations), is also declining. It has become increasingly difficult for the construction industry to bear the expense associated with uncertainty in design and construction practices. Thus, the use of precisely drafted contracts is also being promoted by contractors as a way of protecting limited resources.

Thus, while adaptability in contractual relations remains possible today, many fear this flexibility is waning. In society as a whole, and especially within the ailing construction industry, a more legalistic perspective is developing. Although to date I have seen only minor changes in what is possible on site, there is a greater rhetorical shift; contractors and owners seem more likely to initially resist modifications to original contract documents. Since the loose practices of the past have meant that most projects are bid on basic design drawings and outline specifications, the result is that design development, once enriched by the flexibilities of these contracts, now has the potential to be severely curtailed, since architects cannot effectively push for change on all fronts. Because this shift is one in basic practices, many fear what the future may hold. A recent article in the *Nikkei Weekly*, for example, stated simply, "...the policy of contractual goodwill is coming to an end. The ambiguity of practices seen until now and the breadth of responsibility and liability [held by architects and contractors] is an issue moving towards its conclusion in a impassioned way."

Yet while I have heard a great deal about such limitations, and I witnessed at least one project where the owner, at the request of hostile contractors, attempted to place a moratorium on design development two-thirds of the way into construction, I continue to see refined detailing, customization, and project-specific modifications to building components. It is my sense that the openness to change still found in construction practices will be eroded in the years to come, but that much of what I describe will remain possible in the best work, if only because of the investments Japan's major contractors have made in their reputations for technological sophistication and their commitment to buildings which are well-detailed and constructed.

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