# Case

## The Bull-Dog Sauce Case

(Supreme Court, 7 August 2007) Min-shu Vol. 61 No. 5 p. 2215

**Keywords :** takeover; allotment of rights to purchase new shares without consideration; the principle of shareholder equality; “abusive acquirer"

**[Facts]**

Steel Partners Japan Strategic Fund (Offshore), L. P. (hereinafter referred to as X) is a private investment fund. Steel Partners Japan Strategic Fund—SPVII LLC (hereinafter referred to as A), is a wholly owned special purpose vehicle of X used to purchase shares for X. X invested in many companies in Japan over several years through A. A announced a takeover bid (TOB) to acquire all outstanding shares in Bull-Dog Sauce Co. Ltd (hereinafter referred to as Y). Y’s shares are listed in the second section of the Tokyo Stock Exchange. The original tender offer price by A was 1,584 yen for each share in Y. As of 18 May 2007, the time of the TOB, X held about 10. 25% of the shares of Y. X later raised the tender offer price to 1,700 yen per share.

The reply to questions put by the board of Y to X and its affiliates about the TOB, in the view of the board of directors of Y (hereinafter referred to as “the Board"), lacked concreteness, and was not enough to explain why X bid to acquire all of Y’shares. Therefore, the Board concluded that the TOB could damage the corporate value of Y. The Board decided to propose allotting all shareholders rights to purchase new shares without consideration as a defense measure against the TOB. At a general meeting of shareholders on 24 June 2007 this scheme was approved by 83.4% of attending shareholders’ total voting rights. The allotment of rights to purchase new shares without consideration adopted at the general shareholders’ meeting, was as follows:

1) Y would issue three rights to purchase new shares per existing share to all shareholders;
2) the consideration to be paid by a shareholder for the issue of an ordinary share by Y on the exercise of a right would be 1 yen per share;
3) X and its affiliates, including A, would not be entitled to exercise their rights to purchase new shares; and
4) Y may acquire X’s rights to purchase new shares by paying X and its affiliates 396 yen per right (one quarter of X’s original tender offer price).

There was a risk in relying on the initiative of shareholders to exercise their rights (excluding X and its affiliates). The risk being that some shareholders might not exercise their rights and would not be issued with new shares in proportion to their rights. It was

possible that the Board could not dilute the voting rights of X. Therefore, the Board needed to compulsorily acquire X's rights to purchase new shares to decrease the ratio of shares held by X and to ensure the success of this defense measure.

By Y acquiring the shareholders' rights and issuing new shares to shareholders as consideration, if a certain taxation is imposed on the shareholders under this scheme, since cash is not necessarily delivered to the shareholders, some shareholders have forced the burden of having to sell off their shares for paying tax. Y consulted the Japanese National Tax Agency (NTA) about whether the scheme would give rise to any tax liability. The NTA advised that as the scheme did not generate substantial economic value among shareholders, there would not be any tax liability for shareholders who only received shares. However, X might have a tax liability arising from financial gains under the scheme.

After the approval of the scheme by the general meeting of shareholders, the Board decided that Y would acquire all rights of X and its affiliates at 396 yen per right without causing any tax liability for them (hereinafter, referred to as the "new condition"). Once the scheme was in place the ratio of shares held by X fell from 10.25% to about 3%.

Before the general shareholders' meeting X filed a request for an injunction to suspend allotting the rights to purchase new shares without consideration. X argued that this scheme would contravene the principle of shareholder equality (Art. 109 para. 1 of the Companies Act (Act No. 86 of 2005)); would breach laws and regulations and the articles of incorporation; and was grossly unfair. The Tokyo District Court dismissed X's request (Tokyo District Court, 28 June 2007). X appealed. The Tokyo High Court denied X's appeal after deciding that X was a so called 'abusive acquirer' (Tokyo High Court, 9 July 2007). X then appealed to the Supreme Court of Japan.

**[Judgment]**

The details of the decision of the Supreme Court's Second Petty Bench follow.

(1) The principle of shareholder equality

Article 109 para. 1 of the Companies Act (Act No. 86 of 2005) (hereinafter referred to as the "Act") sets out the principle of shareholder equality and provides as follows: "A Stock Company shall treat its shareholders equally in accordance with the features and number of the shares they hold." ["Stock Company" is hereinafter referred to as "company"].

Even if the allotment of rights to purchase new shares without consideration has the effect of treating rights' holders differently, this does not directly relate to the features of the shares. Therefore, it does not necessarily violate the principle of shareholder equality. However, while shareholders receive the allotment of rights in their capacity as shareholders, Art. 278 para. 2 of the Act provides that the features of the rights to be allotted will be equal. Art. 278 para. 2 provides that a decision about the feature and

number of rights to be issued, or the method for calculating such number, must be in proportion to the number of shares held by a shareholder. Therefore, the principle of shareholder equality, provided in Art. 109 para. 1, will also apply in cases where rights are issued to purchase new shares without consideration.

If a shareholder acquires controlling power over a company and damages its corporate value and harms the interests of the company and the other shareholders, the company may be permitted to treat that specific shareholder differently to other shareholders to protect the company's existence and future development. However, such treatment is not immediately against the principle of shareholder equality unless it is unfair and unreasonable. The decision whether corporate value is damaged or the interests of the company and its shareholders are harmed, should be judged by the shareholders themselves as they own the company. The shareholders' judgments should be treated as definitive unless the facts that formed the basis of their decision were false.

Due to the conditions of the allotment of rights to purchase new shares without consideration, X and its affiliates could neither exercise their rights nor acquire new shares as consideration for their rights. As a result the percentage of X and its affiliates' shareholding in Y would have decreased drastically. However, the scheme to allot rights to purchase new shares without consideration was adopted at the general meeting of shareholders, where X and its affiliates also had an opportunity to express their opinion. As almost all of the shareholders, excluding X and its affiliates, considered it necessary to maintain the corporate value of Y the scheme was approved. Further, according to the contents of the scheme, if X and its affiliates' rights were acquired they would receive cash as consideration. Alternatively, based on the "new condition", if such an acquisition was not exercised, X and its affiliates would receive cash when they transferred their rights to the Board. The cash consideration to be paid by Y was based on the purchase price in the TOB decided by X, and was not unreasonable. Considering the above compensation to X and its affiliates, the allotment of the rights to purchase new shares without consideration did not breach the idea of fairness and does not lack reasonableness.

(2) Is the scheme grossly unfair ?

In this case, because the TOB took place suddenly and there was a real possibility of X acquiring control of Y, the general shareholders' meeting adopted the allotment of the rights to purchase new shares without consideration as a measure to avoid damage to Y's corporate value, not to harm the interests of Y and its shareholders, and to cope with an urgent situation being faced by Y. As mentioned above, as X was able to receive consideration that approximated the value of the rights, though the defensive measures were neither defined nor publicised in advance of the TOB, this scheme was not grossly unfair.

The purpose of the allotment of rights to purchase new shares without consideration,

with discriminatory contents, must be grossly unfair in principle. Such a situation would be where the scheme is not to secure the corporate value and interests of the company and its shareholders, but to maintain the interests of management or specific shareholders who support the management. However, the scheme by Y was not discriminatory and, therefore, not in such a category.

**[Commentary]**

This is the first time the Supreme Court has had to decide on a hostile takeover bid. Hostile takeovers have become a more frequent occurrence in Japan. This decision has great influence on business practices to defend against a TOB, and is of great interest to the legal profession in Japan.

Specifically, Art. 109, para. 1, of the Act is a new provision resulting from company law reforms, and sets down the principle of shareholder equality. This principle also applies to the allotment of rights to purchase new shares without consideration. When corporate value is damaged by a TOB and the interests of the company and its shareholders are harmed, the company is going to oppose the bid. In such a situation, even if the company discriminates against the acquirer, such treatment is not a breach of the principle of shareholder equality unless it breaches the principle of fairness, or is unreasonable.

There is some discussion about whether legally a target company (in practice, its board) can adopt defense measures against a hostile takeover bid. In this case the Supreme Court accepted the legitimacy of a defense measure using the allotting of rights to purchase new shares without consideration. The Bull-Dog Sauce case had the following specific features: Y only adopted the defense measure after the TOB by X was made; and more than two thirds of shareholders approved this defense measure (see Art. 309 para. 2).

The Tokyo District Court dismissed X's request, after admitting that there was discretionary authority for a company to adopt defense measures at a general shareholders' meeting, based on a principle of neutrality of the company's board. The Tokyo High Court considered X as an "abusive acquirer" based on the past activities of X. The Tokyo High Court pointed out that X and its affiliates chiefly pursued profits for the clients of its investment funds and had injured the profits of the other shareholders of companies in which it had invested. However, according to the reasoning of the Tokyo High Court, all investors referred to as general investment funds will be regarded as an abusive acquirer. The reasoning of the Tokyo High Court has received much criticism on this point, and I do not agree with its decision. The Supreme Court was wise not to endorse the decision of the Tokyo High Court.

As mentioned above, the Supreme Court held that the allotment of rights to purchase new shares without consideration with discriminatory conditions is not a breach of the

principle of shareholder equality, when it is necessary and reasonable. However, the scope of application of this decision is not broad. X did not show any plans for management post-acquisition, while attempting to acquire all outstanding shares of Y. Therefore, it seems that the impression formed by each court about X was not necessarily positive because of X's past activities and its reputation. Moreover, in this case, it seems that the decision of each court was considerably influenced by the fact that the general shareholders' meeting overwhelmingly approved the defense measures. But, it is not clear from any of the court decisions on this matter whether under the Act a resolution of the general shareholders' meeting is required to oppose a TOB by putting in place defense measures.

An important issue that can be derived from the three decisions in this case is that placing absolute reliance on the decisions of the shareholders' meeting may have a detrimental effect on corporate value. First, since the existence of voting rights of a general shareholders' meeting are determined as of a specific date ("Record Date"), the potential exists for a shareholder at the Record Date to dispose of their shares before the meeting but still participate at the meeting without having any vested interest in the outcomes of the meeting (Art. 124 para. 1: "A Stock Company may, by prescribing a certain date ("Record Date"), prescribe the shareholders who are stated or recorded in the shareholder registry on the Record Date as the persons who may exercise their rights").

Second, supposing the legitimacy of defense measures depends on a resolution of a shareholders' meeting, then the management needs only to have the resolution passed by the shareholders. As a result, this may lead to the abandonment of management responsibility. This is especially the case where there is a high level of cross-shareholding as management knows this structure would ensure formally passing a resolution of the general meeting of shareholders. In general, in such a situation a company's management cannot be expected to improve corporate value and the interests of shareholders. A company's management has obligations to raise the corporate value and shareholders' investment return, but we must be cautious as corporate value is not always synonymous with improved shareholder returns.

The Corporate Value Study Group of the Japanese Ministry of Economy, Trade and Industry (METI) published a report on 30 June 2008 titled "Takeover Defense Measures in Light of Recent Environmental Changes". In this Report, the Corporate Value Study Group demands company management behaves with responsibility and discipline in the face of takeovers. The Report also requires that management must make decisions by exercising their own judgment, and not simply passing on the decision of supporting or opposing the takeover to the general meeting of shareholders. The company's management must responsibly decide whether or not to adopt and implement takeover defense measures and then fulfill their responsibility of explaining their decision to shareholders. In future takeover cases, it is likely that a focus will be on the effects of any

resolution of the shareholders and the responsibilities of the company's directors.

Postscript: Although X is still investing in some Japanese companies, X sold its remaining shares in Y.

(MURAKAMI Koji and Stephen GREEN)

## Case on the legality of police searching a package delivered to the suspect's residence during the search of the residence under a search and seizure warrant

(The Supreme Court, 8 February 2007) Hanrei-jihō No. 1980, pp. 161-162

**Keywords :** warrant of search and seizure; warrant requirement; delivery; stimulant drug; police; search

**[Facts]**

The accused injected himself with the stimulant phenylmethylaminopropane at his home on around 12 September 2005. In addition, the accused was found in possession of 48.264 grams, a commercial quantity, of a stimulant that was delivered to his residence by a delivery service on 13 September 2005.

At about 13.13 on 13 September 2005, in the presence of the accused, six police searched the accused's residence on suspicion of a violation of the Stimulants Control Act (Act No. 252 of 1951). The police had a warrant of search and seizure that allowed them to search the accused's residence and to seize any stimulants. During the search, the police found 4 syringes, 23 plastic bags, 1 polyethylene bag containing 230 plastic bags, and 1 electronic scale. During the search, at around 14.02, a package that the accused sent to himself was delivered to his residence by a delivery person. The police tried, for about 10 minutes, to persuade the accused to open the package as they wanted to examine the contents. Finally, the police said to the accused, "We need to examine the contents of your package, and we are empowered to examine it. Now we will open your package on our authority." The accused replied, "If you open it on your authority, I will let you have your own way." The police opened the package and found 5 plastic bags containing stimulants. The police arrested the accused for illegal possession of stimulants and seized the stimulant drugs at the location where the accused was arrested.

The accused asserted that the seizure of the stimulants was illegal and the fact of finding and seizing the stimulants was not admissible as evidence. The reason why the stimulants were found was that the package was opened without the accused's consent.

At the first instance trial on 2 March 2006, the court observed on the basis of the exchange between the police and the accused that the accused had consented to the opening of the package. The court found that the seizure of the stimulants was legal, as

examination of the accused's belongings, attendant upon police check-up, is provided for in the Police Official Duties Execution Act (Act No. 136 of 1948). The accused was sentenced to a term of 5-years and 6-months imprisonment and fined 1,000,000 yen. Sixty days of the accused's detention were counted in the accused's imprisonment at hard labor.

On 25 July 2006, the court of appeal judged that the police could open the package on the basis of executing search and seizure on the warrant, even without the consent of the accused, and that it was doubtful the accused had given his consent to the opening of the package. The court dismissed the accused's appeal. The 80 days that the accused was held in pre-sentencing detention pending this appeal was included in the sentence imposed at the trial of first instance.

The accused appealed against the decision. He insisted that the extent of a warrant of search and seizure should be limited to articles that exist in the location to be searched at the time when the warrant was presented to the person it was addressed to. Therefore, the warrant could not cover the package in question, which arrived from another place after the police presented the warrant to the accused.

**[Judgment]**

The main text of the decision of the Supreme Court's First Petty Bench follows.

The Court dismisses the accused's final appeal. The 70 days that the accused was held in pre-sentencing detention pending this final appeal is included in the sentence imposed at the trial of first instance. The Court considers that the accused's counsel's claim in the statement of grounds of the final appeal merely asserts a violation of the law, and a mistake of fact or improper assessment of the sentence that the first instance judged. Further, the accused's claims are merely assertions of a violation of the law or a mistake of fact. Neither the accused's counsel's claims nor the accused's claims come under Art. 405 of the Code of Criminal Procedure (Act No. 131 of 1948).

The Court makes judgment by its own authority.

The facts were found by the court of first instance and are as follows. The police opened the package, delivered to the accused residence by a delivery person and received by the accused, on the basis of a warrant of search and seizure issued on suspicion of the accused violating the Stimulants Control Act (Act No. 252 of 1951). The warrant specified the location that the police should search was the accused's residence and the articles to be seized were stimulants. When the police found stimulants, they arrested the accused for the offense of illegal possession of a stimulant and immediately seized the stimulants. The appellant argued that the scope of the warrant did not extend to the package delivered to his residence after the police served the accused with the warrant. However, the Court considers the decision of the court of second instance in this matter is legitimate, because it is appropriate to construe that the police may also search the package under the same warrant.

Therefore, under Art. 414, Art. 386 para. 1 item 3, and Art. 181 para. 1 proviso of the Code of Criminal Procedure (Act No. 131 of 1948), and Art. 21 of Penal Code (Act No. 45 of 1907), the Court unanimously decides as stated in the text of this judgment.

Chief Justice YOKOO Kazuko, Justice KAINAKA Tatsuo, Justice IZUMI Tokuji, Justice SAIGUCHI Chiharu, Justice WAKUI Norio

**[Commentary]**

One problem with judicial search and seizure (hereafter referred to as "compulsory disposition") in Japan is whether, and if so what situation, the investigating authority is allowed to search an article that does not exist at the place to be searched at the time when the investigating authority presents the warrant to the person, but is brought to the place being searched during the search.

Article 33 of the Constitution of Japan provides: "No person shall be apprehended except upon warrant . . .". The purpose of this article is to inhibit the arbitrary invasion of personal liberty. Article 35 para. 1 of the Constitution of Japan provides: "The right of all persons to be secure in their homes, papers and effects against entries, searches and seizures shall not be impaired except upon warrant issued for adequate cause and particularly describing the place to be searched and things to be seized . . .". Article 218 para. 1 of the Code of Criminal Procedure (Act No. 131 of 1948) (hereinafter "the Code") provides: "A public prosecutor, a public prosecutor's assistant officer or a judicial police official may, if necessary for investigation of an offense, conduct search, seizure or inspection upon a warrant issued by a judge . . .". Article 219 para. 1 of the Code provides: "The warrant set forth in the preceding Article, shall contain the name of the suspect or accused, the charged offense, the articles to be seized or the place, body or articles to be searched, the place or articles to be inspected . . . and the judge shall affix his/her name and seal to it."

Because the execution of a compulsory disposition infringes the fundamental rights of citizens the investigating authority needs the prior approval of a judge. Those fundamental rights include rights associated with ownership of property, and a citizen's right to privacy in their home.

When the investigating authority wishes to execute a search and seizure in relation to the same circumstances, in practice the judge issues one warrant of search and seizure, not two warrants.

A warrant must contain the following three things: adequate cause for its execution; a description of the place; and a description of the body or articles to be searched and seized. It must fulfill all three requirements.

**Adequate cause**

Adequate cause requires that there must at least be the suspicion of an offence, the existence of the article which is the target of the seizure and a relationship with the case. The judge decides whether there is adequate cause.

In this case, the judge who decided to issue the warrant of search and seizure did not know of the particular article, the package delivered during the search, because the police requesting the warrant did not know of its existence when they applied for the warrant.

**Description of the place to be searched**

The reason Art. 35 of the Constitution of Japan, and Art. 219 para. 1 of the Code rigidly provide that the place, body and articles the subject of the search or seizure warrant must be described is that each person's privacy about their body, possessions and their home is protected. For example, the body is protected by personal liberty, and their home and possessions are protected by property rights.

According to previous judicial decisions, there is a problem about whether the investigating authority is allowed to search articles, clothing and the body of a person who is present at the place described in the warrant. The Supreme Court held that the investigating authority can search the traveling bag belonging to B who lives with A, the suspect in another case, based on a warrant of search and seizure describing A's home as the place to be searched (The Supreme Court, 8 September 1994, Keishū vol.48 no.6 p. 263).

In the 2007 case, the court held that, in principle, the investigating authority could search all articles existing in the accused's home at the time the search started because the place described in the warrant was "the accused's home". However, in the case the subject of this note the package did not exist in the accused's home when the investigating authority started the search. In this case, the issue is whether the package that delivered to the accused's home after the execution of the warrant could be searched under the warrant.

**Description of articles to be seized**

There is no provision that the effect of the warrant of search and seizure is limited to articles that exist in the search place at the time the warrant is shown to the accused. According to an earlier case, an article that exists in the place to be searched can be searched, even if the article is not individually described in the warrant (Kyoto District Court, 11 December 1973, Keiji Saiban Geppō, vol. 5 no. 12 p. 1679).

In this case, the issue is whether the stimulants, in the package that was delivered to the search place, are covered by the warrant of search and seizure. Neither the police nor the judge knew about the package at the time of requesting and issuing the warrant, so the judge did not consider the package as an object to be examined when issuing the warrant.

This is the first case in Japan which the courts have had to consider the facts situation where an article was delivered to the search place after the warrant was executed, but before the search was finished.

This judgment is very important as the Supreme Court decided that an article delivered after showing the warrant to the person who is to undergo the measure could be searched by the investigating authority based on the same warrant. This case is important for the practice and the judicial theory of the search and seizure.

However, the Supreme Court did not give detailed reasons in its judgment.

ref. There are some reviews about this Supreme Court's judgment which is written by Japanese;

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(MATSUKURA Haruyo and Stephen GREEN)

## The case of an architect's liability in tort for their design and supervision of the construction of a building that subsequently was found to have defects that infringe the life, body or property of a person

(Supreme Court. 6/July. 2007) Min-shū Vol. 61 No. 5 p. 1769

**Keywords :** damages: torts: building defects: "fundamental safety for a building"

**[Facts]**

In 1988, the original owner of the building the subject of this case (hereinafter cited as 'A') bought land through a real estate agent (hereinafter cited as '$Y_3$'). 'A' contracted with a construction company (hereinafter cited as '$Y_1$') to build a condominium on 'A's land. An architect (hereinafter cited as '$Y_2$') designed and supervised the construction of the building. The building, built from reinforced concrete, consisted of a nine-story part and a three-story part and was for rental accommodation. On 23 May 1990, around three months after construction of the building was completed, a parent and a child (hereinafter

cited as '$X_1$' and '$X_2$') bought the building and the land from 'A'. Transfer of ownership of the land and building was completed on the same day.

In around June 1994, '$X_1$' and '$X_2$' claimed that the building had many defects such as cracks in the corridors, floors, and interior and exterior walls, inclination of beams, insufficient density of concrete, loose balcony handrails, and cracks in drainpipes. They wanted '$Y_1$' either to reconstruct the building, or to return the purchase price, but '$Y_1$' refused both requests. Therefore, on 2 July 1996, '$X_1$' and '$X_2$' sued '$Y_1$' for damages for the cost of repairing the defects pursuant to a warranty against defects and pursuant to the law of torts. '$X_1$' and '$X_2$' also sued '$Y_2$' and '$Y_3$' for damages pursuant to the law of torts. This case note will only discuss the claim for compensation for liability pursuant to torts as it is the most important aspect of the case.

The first trial (Oita District Court, 24 February 2003) dismissed the claim against '$Y_3$' for liability in tort, but found '$Y_1$' and '$Y_2$' liable in tort to pay damages. On appeal (Fukuoka High Court, 16 December 2004; Hanrei-times Vol. 1180, p. 209) the court of second instance denied '$X_1$' and '$X_2$'s claims. According to the judgment of the Fukuoka High Court, a finding that architects are liable in tort was only possible where there is serious illegality such as: where a contractor built a house which was defective intentionally to damage the building owner's rights; the nature of the defects were too inappropriate for society or unethical; or the building itself was a danger to society. The Fukuoka High Court decided that there was no serious illegality in this case.

'$X_1$' and '$X_2$' filed a final appeal.

**[Judgment]**

The main text of the decision of the Supreme Court's Second Petly Bench follows.

This court reverses and remits the judgment of the Fukuoka High Court.

Buildings are used by people who live there, who work there, who visit there, and the like. Additionally, there may be other buildings and roads around them. Therefore, buildings must be safe and not pose a risk to life, body, or property of users of the building, neighbours, people passing by the building, and the like (hereinafter collectively referred to as "residents"). In this situation, the term "safety" should be regarded as the fundamental safety necessary for a building.

Architects, builders, and supervisors of the construction of buildings (hereinafter collectively referred to as "architects/builders") shall, in designing and constructing a building, assume a duty of care to ensure the fundamental safety necessary for the building for residents. This duty exists even if the residents are not a party to a contract relating to the construction or sale of the building. If a building has defects that undermine the fundamental safety necessary for a building because of the architect's/builder's breach of their duty of care and the defects infringe life, body, or property of residents, the architect/builder shall be liable to compensate for the damage as tortfeasors. However,

this shall not apply to special circumstances such as where residents, claiming the liability in tort, knew about the defects before buying the building.

In addition, the existence of defects affecting the fundamental safety necessary for a building is enough for architects/builders to be liable in tort. There is no reason to limit liability in tort only to cases where the illegality is serious. The court of second instance erroneously construed Article 709 of the Civil Code (Act No. 89 of 1896) and this misconstruction affected the judgment. This court remits this matter to the court of second instance to further examine whether the building has defects that affect the fundamental safety necessary for a building and if such defects exist, they shall consider whether the defects infringe the life, body, or property of residents, and whether the architects/builders must pay compensation for the damage as tortfeasors.

**[Commentary]**

This judgment is problematic; it says that '$Y_1$', '$Y_2$', and '$Y_3$' violated '$X_1$' and '$X_2$' by the infringement of '$X_1$' and '$X_2$'s right to own a properly constructed building (hereinafter referred to as "ownership rights") by tortious acts. Initially, '$X_1$' and '$X_2$' wanted '$Y_1$' to reconstruct the building or return the purchase price. Because '$Y_1$' refused to do either of these things, '$X_1$' and '$X_2$' sued '$Y_1$', '$Y_2$', and '$Y_3$'. In the first trial their main claim was for compensation for repairing the defects and compensation for damages suffered by their business. These should be claimed against 'A', the vendor, under the warranty against defects in the contract for the sale of the land and building. However, 'A' was insolvent, so '$X_1$' and '$X_2$' sued '$Y_1$', '$Y_2$', and '$Y_3$' whose financial position was relatively secure.

As previously noted, this judgment said that '$Y_1$', '$Y_2$', and '$Y_3$' violated '$X_1$' and '$X_2$' by the infringement of '$X_1$' and '$X_2$'s ownership rights by tortious acts. However, '$Y_1$', '$Y_2$', and '$Y_3$' were responsible for the design, construction and sale of the building with its defects, and the building was then bought by '$X_1$' and '$X_2$' from 'A'. This is not a case which clearly involves infringement of ownership rights by tortious acts such as '$Y_1$', '$Y_2$', and '$Y_3$' destroying the building owed by '$X_1$' and '$X_2$'. The state of the building due to its defects is the important point in this case, and it cannot be said that the architects'/builders' tortious acts intentionally or negligently infringed the rights of ownership of the eventual owners, '$X_1$' and '$X_2$'.

If the infringement of ownership rights by a tortious act is accepted in this case, there is still another problem that remains. The judgment says that if the building had defects which affected the fundamental safety necessary for a building because of the architects'/builders' breach of their duty of care, and this breach infringed the life, body, or property of residents, the architects/builders are liable to pay compensation for the damage as tortfeasors. In contrast, '$X_1$' and '$X_2$'s main claim was for damages for the immediate costs to repair the defects, and to compensate them for damage to their business. It is possible that '$X_1$' and '$X_2$' may suffer loss in the future for example if a third person or

third person's property was injured or damaged as a result of a defect in the building. However, no such event had occurred and '$X_1$' and '$X_2$' did not raise this as an issue in the Oita District Court trial. Infringement of ownership rights, which '$X_1$' and '$X_2$' claimed seem to be different from the rights which the court found.

The judgment said buildings shall have a level of safety so as not to be a risk to the life, body, or property of residents and the term "safety" should be regarded as the fundamental safety necessary for a building. The key phrase "the fundamental safety necessary for buildings" is not mentioned in the Civil Code. The safety level which all buildings should have may mean that they must not be a risk to the life, body, or property of residents. In future it will be necessary to specify which buildings lack the fundamental safety necessary for buildings and which buildings do not. This judgment is likely to be the subject of future consideration and comment by lawyers, professors, and judges.

Although not without some problems, this judgment is of great importance. It clearly establishes that architects/builders have a duty of care to ensure the fundamental safety necessary for a building and that duty is owed to residents even if they are not in a contractual relationship with the architect/builder. This judgment overturned the Fukuoka High Court decision not to find '$Y_1$', '$Y_2$', and '$Y_3$' liable based on earlier decisions that the liability of architects/builders in tort for building defects is limited.

Furthermore, this judgment clearly states that the existence of the defects threatening the fundamental safety necessary for a building is enough to establish the liability of architects/builders in tort and there is no reason to only limit liability to cases where the illegality is serious. By saying this, the court implied that residents should have legal protection from the risk to life, body, and property in such situations.

Japanese courts have considered similar cases. In one case a purchaser found his new building did not comply with the Building Standards Act (Act No. 201 of 1950), so he canceled the contract and sued the vendor, the architect, and the builders for compensation under tort law. The court of second instance in that case (Osaka High Court, 7 November 2001; Hanrei-times Vol. 1104, p. 216) said people who construct buildings must obey the rules of the Building Standards Act and must not place at risk others' life, health, or property. If they offend against the law violating others' property and cause them damage, they will be liable for compensation under the law of torts.

In another case a claim for compensation was made against the builders who were contracted to construct a building (Kobe District Court, 8 September 1997; Hanrei-times Vol. 974, p. 150). The court decided that a land owner that enters a building contract and third parties claiming liability in tort against contractors would only be admitted in special cases where the illegality was serious, for example, where a contractor built a defective house intentionally to damage the property owner's rights and profit. The Fukuoka High Court, in the matter which is the subject of this case note, took the same approach as the Kobe District Court.

The decisions of the Osaka High Court and the Kobe District Court reflect established values about the level of liability that architects/builders should have. However, recently there are many cases where certification of earthquake-proof construction has been falsified and recovery of losses suffered by an aggrieved party is an important issue. The decision that architects/builders may be held liable to pay compensation sought by residents, where their house is found to have defects, even if they are not in a contractual relationship with the architect/builder, where their house is found to have defects reflects the expectations of society.

(KIDO Akane and Stephen GREEN)