Interim Report Pertaining to "Future Measures against Violations under the Act against Unjustifiable Premiums and Misleading Representations, Including Introduction of a Surcharge System"

April 1, 2014

Consumer Commission
Expert Panel for Surcharge System, etc. against Misleading Representations under the Act against Unjustifiable Premiums and Misleading Representations, Consumer Commission

1. Introduction

In response to the consultation made by the Prime Minister with respect to "future measures against violations under the Act against Unjustifiable Premiums and Misleading Representations (Act No. 134 of 1962; hereinafter referred to as the "Act") including introduction of a surcharge system, etc. in order to ensure the effectiveness of regulations over misleading representations under the Act," the Consumer Commission established on December 9, 2013 the "Expert Panel for Surcharge System, etc. against Misleading Representations under the Act against Unjustifiable Premiums and Misleading Representations"; the Expert Panel initiated the investigation and discussion from February 2014 and its sessions have in principle been held at the same time as plenary sessions.

Thus far 6 sessions were held, where the results of deliberation by the "Study Group for Administrative Methods for Consumer Property Damage" of the Consumer Affairs Agency (hereinafter referred to as the "Study Group for Administrative Methods") and subsequent progress of the deliberation were explained and the need for introduction of a surcharge system and the purport, purpose, conditions(legal requisite), procedures, etc. of the system, if actually introduced, were discussed. Also, hearings were conducted in order to hear opinions of business operators and to refer to the operations of existing surcharge systems[1].

Under the investigation and discussion conducted until now, we have run through most of the issues, which are relevant to the introduction of a surcharge system under the Act and for which the Consumer Affairs Agency provided explanation based on the

[1] Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (Act No. 54 of 1947), Financial Instruments and Exchange Act (Act No. 25 of 1948) and Certified Public Accountants Act (Act No. 103 of 1948).

results summarized by the Study Group for Administrative Methods, except for the issue of how we should design the system from the viewpoint of damage recovery (it has been determined that this issue will be separately discussed after the conditions, procedures, etc. are deliberated, as described later); in order to further deepen the deliberations in the future, this interim report sorts out the progress of deliberation on each issue.

2. Need for introduction of a surcharge system under the Act

The panel members have a unanimous view that there is a substantial need for introduction of a surcharge system under the Act.

The main views can be summarized as follows. First, it is pointed out that the number of consultations about consumer damage received by the National Consumer Affairs Center, which were caused by misleading representations or advertising, has climbed to about 50,000 cases a year (according to the “Annual Report on Consumer Affairs 2010” and “Annual Report on Consumer Affairs 2013” by the National Consumer Affairs Center, the number of consultations whose main subjects were “representations and advertising” has been exceeding 40,000 cases every year since 2004, and the number was 49,492 cases in 2012), and that the percentage of the consultation cases involved with “representations and advertising” seems to be increasing, considering that the total number of consumer consultation cases has been decreasing. It is also pointed out that, even though not all consumer damage cases were directly caused by misleading representations or advertising, many of these cases can actually be attributable to misleading representations or advertising, because there are so many transaction types (such as Internet shopping services, whose users have been increasing in the last several years) in which consumers make decisions about products and services only based on advertising when entering into transactions, and it is believed that the actual number of consumer damage cases caused by misleading representations should become far more than 50,000 cases a year, if the potential cases of misleading representations, though not classified as such, are included.

It is further indicated that many of the damage cases caused by misleading representations are, by their nature, not suited for civil lawsuits, because individual consumers would have difficulty in calculating damages they have suffered when it is difficult to establish a causal relationship in a damage case caused by misleading representations and when the damage itself cannot easily be made clear, and also because the damages amount would become too small, even if successfully calculated. Some also indicate that, in many of the damage cases caused by misleading

representations, damages cannot properly be compensated once suffered by consumers. The fact that consumers have difficulty in recovering damages means that business operators, which have committed misleading representations, still retain, without condemnation, the profits obtained from the sales generated through the commitment of misleading representations. The cease and desist order under the current Act aims to suspend the misleading representations by violators prospectively in order to prevent spread and recurrence of damage, but it does not deprive the violators of their unfair profits and, from an economic perspective, it does not effectively deter the violations. For this reason, some consider that the surcharge system should be introduced, in addition to the cease and desist order. Some further indicate a concern that, unless a violator is deprived of its profits generated by the time of the accusation of a misleading representation, then other business operators would follow the violating practice even when they have been providing consumers with fair product information, and such consequence would create disadvantages not only for the direct victims of the misleading representation but also for all consumers. There is also an opinion that, from the viewpoint of ensuring fair treatment of business operators which comply with laws and regulations and ensuring consumer benefit based on the compliant practices by the business operators, it is extremely important to introduce the surcharge system, which imposes an economic disadvantage on the violators, in order to prevent the business operators, which have acquired customers through misleading representations, from retaining their unfair profits without condemnation.

As described above, the panel members have a unanimous view that there is a need to introduce, as a policy measure mainly to deter misleading representations, the surcharge system, which counteracts the incentives to commit violations by imposing economic disadvantages on violators.

In this regard, at the hearings from business operators, some business operators stated that they basically understand the need to develop some sort of system, including the surcharge system. On the other hand, some other business operators questioned whether or not clarity of regulatory conditions for misleading representations will be ensured in every product area, and pointed out that if an excessive regulation is enforced with malicious business operators in mind, then it will intimidate honest business operators and especially there will be a fear of small and medium sized enterprises being negatively affected by it; however, some business operators expected that the deterrent power of the surcharge system will maintain consumer transactions at a healthy and sound level.

3. Purport and purpose of the surcharge system, if actually introduced

The panel members have a unanimous view that the main purpose of the surcharge system is to deter misleading representations.

In addition to this, it was also discussed whether or not recovery of damage should be included as part of the purpose of system, while considering that recovery of damage is in reality difficult in misleading representation cases. Some argued that the perspective of consumer damage recovery should not be excluded from the discussion on the conditions, procedures, etc. of the surcharge system, based on such reasons as that the Act is positioned as a consumer law and that the unfair profits generated by business operators are originally derived from payment by consumers. Basically, however, it has been decided that measures to recover consumer damage will separately be deliberated, after deliberation on the conditions, procedures, etc. of the surcharge system.

In this regard, at the hearings from business operators, some business operator stated that the purpose of the surcharge system should be limited to deterring violations and the issue of damage recovery should be considered separately.

4. Conditions for imposition of a surcharge

(1) Surchargeable cases

(a) Surchargeable acts

Deliberations covered the issue of whether or not misrepresentations of the better or more advantageous quality, representations designated by public notice, or representations regulated as unproven advertisements should be subject to imposition of the surcharge. There is a consensus that the misrepresentations of the better or more advantageous quality should be subject to imposition of a surcharge, and a consensus was generally reached that the representations designated by public notice should not be subject to imposition of the surcharge, considering that the representations designated by public notice themselves are not misrepresentations of the better or more advantageous quality but have been regulated for a preventive purpose.

On the other hand, there was a difference of views as to the issue of whether or not the representations regulated as unproved advertisements should be subject to the surcharge, although there was no opinion which proactively opposed the imposition of a surcharge on such representations.

First, there were views which proactively approve the imposition of a surcharge, based on such reasons as that when business operators draw more customers by engaging in a certain misrepresentation of the better or more advantageous quality

without data showing reasonable grounds for the representations, such conduct of business operators is highly malicious and there is a need to deprive the business operators of their unfair profits generated from the transactions; that if there is no imposition of a surcharge, then there might be a situation where business operators would not submit the data showing reasonable grounds for the representations and would just receive the cease and desist order only, without the surcharge being imposed on them; or that as a rule of conduct to be observed by business operators, they should engage in representations of their products or services after acquiring beforehand certain data showing reasonable grounds for the representations.

On the other hand, some indicated that more careful deliberations are needed for the issue of whether or not the representations regulated as unproved advertisements should be subject to the surcharge, given that if the representations regulated as unproved advertisements become subject to the imposition of a surcharge, then the surcharge will be imposed on a business operator because it “has failed to submit the data showing reasonable grounds for its representation,” or in other words, because of a sort of violation of procedures, and as a result a new category of misrepresentations will be created with different characteristics from those of the existing category of misrepresentations. It was further indicated that, if the surcharge is imposed on the representations regulated as unproved advertisements, which are not substantively the same as the misrepresentations of the better or more advantageous quality, there will be a problem of whether the decision to impose the surcharge on a representation regulated as an unproved advertisement may be revoked or not if reasonable grounds for the representation are submitted during the action for revocation of the imposition of a surcharge after an appeal is entered against the imposition. In response to these indications, some stated that there is no need to conclude that the representations regulated as unproved advertisements are a new category of misrepresentations or that the decision to impose a surcharge cannot be revoked in an action for revocation; but rather, when introducing new provisions, it can be prescribed that the representations regulated as unproved advertisements can tentatively be considered as misrepresentations of the better or more advantageous quality and be subject to the order for payment of a surcharge, and that the decision to impose a surcharge may be revoked if data showing reasonable grounds is submitted at the stage of an action for revocation.

Some expressed an opinion that they would like to deliberate the issue of whether the representations regulated as unproved advertisements should be subject to the surcharge or not, based on results of discussion on other conditions to be introduced,

thus it will be necessary to continue the deliberation on this issue after the issuance of this interim report.

In addition to the above, there is a request that the conditions for imposing the surcharge on the misrepresentations of the better or more advantageous quality, for which a consensus was reached on the imposition of a surcharge, should be clarified as far as possible through establishment of guidelines, etc., so that business operators will not unnecessarily be intimidated.

(b) Subjective factor

Deliberations covered the issue of whether or not any subjective factor should be required as a condition for the imposition of a surcharge on a violation, and if hypothetically such factor is required, how its substance should be considered.

In this regard, there is an opinion that the subjective factor should not be a condition, given that consumer damage would be caused by misrepresentations regardless of whether or not the violator had willful intention or negligence and that profits generated by the violator from such misrepresentations are nonetheless unfair profits from the perspective of consumers; it is also pointed out that a subjective factor is usually not required in the cases of administrative dispositions. However, numerous members preferred an eclectic approach, based on the basic recognition that a subjective factor should be required in light of the purpose of deterring misrepresentations; they suggest that in principle the subjective factor should be deemed to be satisfied when a misrepresentation exists, and that exemption from the imposition of a surcharge will apply as an exception if lack of the subjective factor is demonstrated.

Notably, some indicated a need for a subjective factor, based on the reason that the surcharge system cannot effectively deter violations in cases when a misrepresentation comes to exist from an objective point of view despite the fact that a business operator has exercised adequate care, i.e. the business operator has committed no negligence, and that in such case the purpose of law cannot be achieved; at the same time, it was suggested the government will have difficulty in proving the subjective factor. It was also stated that, considering that the misrepresentations are confined to “significant” misrepresentations upon recognition of the “misrepresentations of the better or more advantageous quality,” willful intention or a remarkable lack of care required under socially accepted conventions must exist in many of the misrepresentation cases, and therefore it would be sufficient to exclude, as an exception, the cases when business operators provide reasonable counter-evidence.

On the other hand, it was also argued that, if a supplier has supplied to a business operator raw materials that do not match with the representation despite the fact that the business operator has been exercising adequate care, and if the surcharge is inevitably imposed on the business operator without considering the subjective factor, then it would be unreasonable because the business operator retains no unfair profits and will even be required to pay the surcharge while it has already suffered loss of its brand value and reputation. In response to this argument, there was a counterargument that, even in such cases, the business operator had an opportunity to check the supplies in advance, and that it would be unreasonable if the risk of damage is attributed to consumers, because consumers will have more difficulty in claiming compensation for damage than the business operator will.

At the hearings from business operators, there was an opinion that the surcharge system should only target highly malicious cases, and that if the system only targets the misrepresentations with willful intention or gross negligence, the business operators will be able to feel secure in conducting business activities. In response, however, a panel member suggested that negligence in a much wider sense should rather be used as a condition for imposition of a surcharge, based on such reasons as that the determination of whether negligence is a minor one or a gross one is often difficult in civil litigation practices when examining the subjective factor; that if gross negligence is set as a condition for imposition of a surcharge, then accused business operators would surely excuse themselves by saying “we didn’t know,” “we have paid sufficient attention,” etc. and it would be difficult to impose the surcharge on them under the imposition procedures, in which recognition of negligence is made by administrative authorities and for which swiftness is required; or that the risk of misrepresentation damage caused by minor negligence should not be attributed to consumers.

In addition to the above discussion of the subjective factor, questions were raised with respect to the cases when more than one business operator is involved in a misrepresentation; the questions included how the scope of business operators to which the surcharge will be imposed should be defined, and with respect to which business operator the subjective factor should be considered.

(c) Criteria based on size

The discussion also covered the issue of whether or not the surcharge should be imposed even when its amount becomes less than a certain level (the issue of “cutback”). Some suggested that, because many misrepresentations are committed by small-sized business operators or individuals, a surcharge should be imposed

whenever damage is caused by a misrepresentation, regardless of whether the size of damage is large or small; however, a consensus was generally reached that a certain amount of cutback is necessary, with consideration for the burdens of law enforcement, etc.

It was also suggested that the base amount of cutback should be set in a careful manner in order to maintain the effect of the surcharge system and with consideration for the size of social impact of the violation and subjective aspects of the violator, and that at least 70 to 80% of the cases, for which the cease and desist orders are issued, should be subject to the imposition of a surcharge.

(d) Statutory exclusive period

A consensus was generally reached that a certain reasonable period should be set as a period of exclusion.

(2) Calculation of surcharge amounts

(a) Basic concept

With respect to calculation of surcharge amounts, there were discussions, in light of the purpose of a surcharge system, about how to determine the surcharge amounts necessary and sufficient to secure the deterrent effect on violations, and the reasonable calculation method for the surcharge amounts. In order to deter violations intentionally committed, the amount of the surcharge should be equal to or more than the amount of unfair profits generated by the violator; some suggested that the amount of the surcharge should in principle be determined based on the amount of the unfair profits generated by the violator, on the premise that the same criterion will be used for both the case of willful intention and the case of negligence, considering the difficulty in proving the willful intention. Also, a consensus was generally reached that, in calculating the amounts of the surcharge, the unfair profits should be calculated in a uniform manner in order to ensure administrative efficiency, and not for each individual case, although the unfair profits may be different depending on profit margins and services in each transaction.

It was suggested that the calculation method of unfair profits should be deliberated taking into account the revision bill of 2008[2]; under this revision bill, a ratio was set in reference to the operating profit margins of individual business operators and then the sales generated from the products or services which become the subjects of

[2] "A bill for the Act on Partial Revision of the Act on Prohibition of Private Monopolization and Maintenance of Fair Trade and the Act against Unjustifiable Premiums and Misleading Representations." Under this bill, the system of a surcharge against misrepresentations under the Act was incorporated; the bill was submitted to the Diet in March 2008, but eventually was discarded.

violation were multiplied by the ratio. In this regard, it was also pointed out that consideration should be paid when the sales generated from the products or services which become the subjects of violation are used as a criterion, because a dispute is easy to occur over the scope of such products or services; there was another opinion that the past violation cases should be closely investigated and then further examination should be made as to whether or not the calculation method is reasonable enough.

Under the revision bill of 2008, the calculation method of the surcharge was defined as “the sales generated from the products which become the subjects of violation × 3%”; however, there is an opinion that such calculation ratio cannot have an adequate deterrent effect expected of the surcharge system, and that the calculation ratio of at least 10% should be considered, with consideration for the regulation of unreasonable restraint of trade, etc. under the Act on Prohibition of Private Monopolization and Maintenance of Fair Trade.

(b) Addition to the surcharge, subtraction from the surcharge or exemption of the surcharge

The discussion covered addition to, subtraction from, or exemption of the amount calculated under (a) above. As for the additional surcharge, there was an opinion about the reasons for addition, but some suggested that the legislative facts must be examined; there is room for future discussion as to whether an additional surcharge should be introduced or not. A general agreement was reached that discussion into introducing subtraction from the surcharge and exemption of the surcharge are to be continued.

The discussion also covered the possible details of such measures; first, with respect to the introduction of addition, subtraction or exemption from the perspective of business operators’ compliance, there was an opinion that if an act which cannot be overlooked from the perspective of compliance exists in the process of violation, then such act may be a reason for addition to the surcharge. On the other hand, while it was suggested that we should consider allowing subtraction from the surcharge according to whether or not a compliance system is established, or the level of such a compliance system, there was an argument, however, the fact that business operators naturally owe the duty of compliance and the level of compliance is not an appropriate reason for subtraction from the surcharge, or that management has a wide range of discretionary power for establishment of a compliance system and there is a concern that the surcharge system would be rendered ineffective if subtraction is easily permitted.

It was also suggested that intentional violations, recurring violations and cover-ups of violations including cover-ups of whistleblowing may, for the time being, be considered as reasons for addition to the surcharge, in order to enhance the deterrent effect of the system. Some stated that subtraction and exemption should also be proactively deliberated as an incentive for self-declaration, or that voluntary reimbursement from business operators, donations to public institutions, etc. may be considered as reasons for subtraction or exemption, from the perspective of damage recovery. On this point, it was also suggested that, while the subtraction and exemption may be effective measures for facilitating earlier declarations of violations and reimbursements to victims, consideration must be paid for the relationship with the deterrent effect of the surcharge system when setting the conditions for such measures, and deliberations should continue on such issues as on what basis the conditions should be set or what sort of framework is conceivable in order to properly recognize fulfillment of the conditions.

In this regard, at the hearings from business operators, it was suggested that a measure to adjust the surcharge amount according to the amount of reimbursement, while respecting voluntary actions taken by business operators.

(c) Applicable period

A consensus was generally reached that the period subject to calculation of the surcharge should be limited to a certain reasonable period. Some suggested that a period of about 5 years may be appropriate, considering that the period of 3 years, as prescribed in the revision bill of 2008, is too short.

(3) Adoption of discretionary power of administrative authorities

The discussion also covered the issue of whether or not discretionary power of administrative authorities should be adopted for the surcharge system; while some suggested that adoption of discretionary power should be considered from the viewpoint of preventing excessive increase of burdens associated with law enforcement after introducing the surcharge system and consequent hindrance to the enforcement of the current cease and desist order, a consensus was generally reached that we should be careful in adopting the discretionary power from the viewpoint of ensuing predictability, transparency, fairness and swiftness. It was pointed out that discretionary power of administrative authorities should be excluded as far as possible, because the Act widely applies to representations in general and the Act should be enforced in an objective manner, and that we should be careful in regard to forthright adoption of the discretionary power because the burdens associated with law

enforcement may be addressed by placing a certain limitation on target cases through the setting of other conditions and by applying addition, subtraction and exemption based on certain criteria.

5. Procedures for imposition of a surcharge

Some suggested that the surcharge should be imposed on violation in accordance with more careful procedures than the procedures for the cease and desist order; however, a consensus was reached that, considering objectivity of target violations, etc., there is no need to specially introduce stricter procedures, and that there will be no problem if the same procedures as taken for the cease and desist order under the current Act are adopted.

With respect to enforcement, it was pointed out that role-sharing and collaboration between the national government and prefectural governments should be further deliberated, taking into account the measures for strengthening of administrative monitoring and guidance under the bill to amend the Act, etc., which has been submitted to the current Diet[3].

6. Conclusion

The above is the summary of deliberations made on each issue, through the investigation and discussion up to the 6th session.

Based on this interim report, we will conduct more hearings from business operators, etc. and continue the investigation and discussion on the issues which are thought to require further deliberations, including the issues already deliberated.

Especially, with respect to the future measures for recovery of damage as described above, we should keep in mind that during the discussion up to now multiple panel members pointed out that individual consumers often have difficulty in recovering damage suffered in misrepresentation cases and that it is important to have the perspective of damage recovery when we deliberate the introduction of the surcharge system. Originally, the collected surcharge should be returned to the consumers who are the victims; there was an opinion that it is desirable to establish a framework under which the collected surcharge will be returned to general consumers in some way, while considering that it is difficult, from a practical perspective, to design a system in which the collected surcharge will be distributed to individual victims, because damages should originally be recovered by means of civil litigations and also because the

[3] "A bill for the Act on Partial Revision, etc. of the Act against Unjustifiable Premiums and Misleading Representations, etc."

damages is difficult to be calculated and may become too small even if successfully calculated. On the other hand, at the hearings from business operators, there was an opinion that the surcharge should belong to the national treasury; we will arrange another opportunity for sufficient discussion on this issue, after deliberation of the conditions, procedures, etc.

(End of document)