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An Introduction to Economic Approaches to Damages in a Japanese Context

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I. Introduction

Damages awards like the 2008 order for USEN Corporation to pay ¥2,052 million to Can System Corporation[2] raise questions about how damages awards are assessed and how they connect to allegations in Japanese courts. Currently, the Code of Civil Procedure 248 permits courts to determine award amounts without employing scientific methods when it is not feasible for plaintiffs to calculate damages in a scientific manner,[3] regardless of the amount. As scientific approaches tie damages awards to the facts of a case, increasing the use of these methods in Japanese courts could lead to more equitable damage award amounts. In this article, we introduce a framework[4] used for calculating actual (loss-based) and restitution (gains-based) damages in the United States and other countries, and some of the practicalities and resources involved in implementing an economic approach to damages. We then discuss how damages are currently assessed in Japan, and opportunities to employ economic approaches. We hope this may be compelling for parties interested in affirmatively proposing or

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[2] These damages were awarded in response to allegations of USEN (1) using false information to poach (aggressively recruit from a competitor) a large number of employees from Can System and (2) offering discriminatory pricing (a special discount to a competitor's customers to exclude the competitor from the market) to Can System customers. USEN vs. Can System Corporation. (Tokyo District Court, December 2008), 1288 *Precedent Times* 112 (2009). Private monopolization and unreasonable restraint of trade is restricted by *The Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (The Antimonopoly Act, AMA): Chapter II Private Monopolization and Unreasonable Restraint of Trade*, available at https://www.jftc.go.jp/en/legislation_gls/amended_ama09/amended_ama15_02.html. Discriminatory consideration is considered an unfair trade practice by the JFTC. See *Designation of Unfair Trade Practices*, Fair Trade Commission Public Notice No. 15 (June 18, 1982), available at https://www.jftc.go.jp/en/legislation_gls/unfairtradepractices_files/unfairtradepractices.pdf.

[3] *Legal Term Glossary*. City-Yuwa Partners, http://www.city-yuwa.com/explain/ex_glossary/detail/songaigaku.html (last visited July 25, 2018). Note that comparing financial outcomes before and after the cartel period is considered appropriate by Japanese courts. Kozo Kawai and Madoka Shimada, Japan, in *The Private Competition Enforcement Review* 157–168, (Ilene Knable Gotts , ed., 5th ed. 2012), available at https://www.jurists.co.jp/sites/default/files/tractate_pdf/ja/1009_kawai_japan_chapter.pdf, p. 164.

[4] Note that there are multiple potential methods that may be applied within this framework, the details of which are outside the scope of this article and the appropriateness of which may depend on the details of the case..

challenging damages amounts in Japanese courts, such as defendant or plaintiff decision-makers and their counsel. Additionally, Japanese firms may be exposed to lawsuits in other jurisdictions, including the US courts, so understanding an approach used abroad may be helpful in navigating legal landscapes and litigation risk outside of Japan.

II. An Economic Framework for Actual Damages

The definition of actual ("compensatory") damages seems straightforward: "money awarded to compensate for actual losses."[5] It appeals to a concept of justice where the injured party is made whole in a form that is easily transferred between parties (i.e., money). The simplicity of actual damages, however, is conceptual; implementation raises several empirical questions specific to each case:

(1) What happened to the plaintiff[6] as a result of the alleged harmful act?
(2) What would have happened to the plaintiff had the alleged harmful act not occurred?[7]
(3) How can the difference between the outcomes in (1) and (2) be monetized?

We refer to (1) as the "actual world," which is what actually happened to the plaintiff. Since this corresponds to actual events, some information may have been collected in the ordinary course of business, such as invoices for sales or purchases, medical records for treatment after an injury, and correspondence. This information may be obtainable, although it may be incomplete or in a form that is difficult to interpret. Moreover, given that some of the information is held by defendants and some by plaintiffs, it can be subject to an involved discovery process.

Understanding what would have happened in (2), the "but-for world," is a more complicated question. Since these events never occurred, they must be simulated. The simulation needs to be grounded in the facts of the case, and it can involve using the available information and economic and statistical models to estimate what would have taken place but-for the alleged bad act. For example, in a price-fixing case where defendants are alleged to have set prices through secret meetings, an economist would need to estimate what prices

[5] *Actual Damages*. Cornell Law School Legal Information Institute, Wex, https://www.law.cornell.edu/wex/actual_damages (last visited May 31, 2018). Other forms of damages, such as punitive damages, are beyond the scope of this article.
[6] We refer to a singular plaintiff, but there may also be multiple plaintiffs in a case, such as in American consumer class action cases.
[7] See, e.g., *Quantifying Damages*, in *Proving Antitrust Damages* (2nd ed., 2010), p. 53.

would have been in the but-for world without the alleged conspiracy. When outcomes are not in monetary terms, the analysis may also involve estimating the monetary equivalent of the difference in outcomes based on available information or comparisons to publicly available data. Similarly, in a wrongful termination case, where a plaintiff is alleged to have been terminated by an employer in the breach of his contract of employment, lost earnings may be offset by the expected value of the plaintiff getting another job in the actual world, calculated using government data on the earnings of individuals with similar characteristics. Economists are well suited to the role of presenting a scientifically tenable but-for world, as they have advanced training applying econometrics, which is "the science and art of using economic theory and statistical techniques to analyze economic data."[8]

The "actual" and "but-for" world-framing may also be applied to calculating restitution damages, which, in civil cases is "[a] remedy associated with unjust enrichment in which the amount of recovery is based on the defendant's gain rather than the plaintiff's losses."[9] To isolate the unlawful gains, which are the profits obtained by the defendant as a result of the alleged conduct, one calculates the difference between the defendant's actual and but-for profits. Conceptually, this unlawful gains approach is equivalent to replacing "plaintiff" with "defendant" in (1) and (2) above.

These general damages concepts apply in a variety of cases, including those related to price-fixing, bid-rigging, exclusionary private monopolization,[10] pay-for-delay, wrongful termination, false advertising, and intellectual property infringement, although techniques and approaches may vary between applications. Taking an exclusionary private monopolization case as an example, damages amounts could be calculated such that they compensate for the difference in profits earned by the plaintiffs when the alleged firm did not prevent the plaintiffs from operating in the market ("but-for profits") and when the alleged firm attempted to exclude the plaintiffs from the market ("actual profits"). These concepts and techniques may be applied at different stages of a case, and not just formally in expert damages reports. For

[8] James H. Stock and Mark W. Watson, *Introduction to Econometrics* 3 (2003).
[9] *Restitution Damages*, Cornell Law School Legal Information Institute, Wex, https://www.law.cornell.edu/wex/restitution (last visited August 12, 2018).
[10] The JFTC defines exclusionary private monopolization as "[e]xcluding the business activities of other entrepreneurs, thereby causing, contrary to public interest, a substantial restraint of competition in any particular field of trade." JFTC. *The Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act.* (October 28, 2009), available at https://www.jftc.go.jp/en/pressreleases/yearly-2009/oct/individual-000036_files/2009-Oct-28_2.pdf.

example, preliminary analyses to gauge potential damages awards could be used in decision-making to enter into litigation or as a resource in settlement negotiations.

From a public policy perspective, fines for illegal conduct are both an enforcement tool and a mechanism to prevent firms from committing illegal acts. From a cost-benefit perspective, it could be beneficial to a firm to commit an illegal act up to the point that the expected cost of punishment (e.g., fines, sanctions or litigation) exceeds the unlawful gains from committing the illegal act. If fines are set too low, committing the harmful act is profitable even though the fine must be paid, so firms have an incentive to commit harmful acts. Thus, the authorities may consider setting fines at least at a level such that expected losses from detection exceed the incremental profits obtained from engaging in the illegal activity,[11] so scientifically calculating potential unlawful gains may be useful in arriving at and setting optimal fine levels.

III. Assessment of Damages in Japan and Opportunities for Applying an Economic Framework

The application of economic methods in antitrust litigation has been stagnant in Japanese courts due to relative inactivity in antitrust civil litigation unrelated to bid-rigging.[12] The number of litigated bid-rigging cases is also expected to decrease because of the practice of including penalty rules for antitrust violations in contracts. This practice may reduce litigation because penalty rules specify how behavior that violates a contract will be penalized in advance, so parties in violation of antitrust laws will trigger penalty rules and the punishment will be enforced outside of court according to the terms prescribed in contracts. This practice of incorporating penalty rules in contracts started in 2003 after the Ministry of Land, Infrastructure, Transport and Tourism introduced a penalty provision in their contracts.[13] A common penalty level for an allegedly harmful act is 10% of the ordered value,[14] following the amount recommended by the Ministry of Land, Infrastructure, Transport and

[11] Some readers might think that fines could be set infinitely large to deter harmful conduct. However, fines that are too large may have some negative consequences to society and stakeholders of the firms such as bond holders, stock holders, and employees, if the firm goes bankrupt through paying fines (Wouter P.J. Wils, *Optimal Antitrust Fines: Theory and Practice,* 29 World Competition, 1, 20 (2006)).
[12] Mamoru Izumisawa, *The Antimonopoly Act and Damages Claims Litigations,* 16 Contemporary Law Study 3, p. 5 (2008).
[13] Masahiro Murakami, Supervising Editor, *The Antimonopoly Act and Private Enforcement of Actions for Damages and for Injunction* (2018), p. 44. ("Murakami")
[14] The ordered value can be thought of as the volume of commerce, in yen or another currency, at issue.

Tourism. Setting a penalty level in the initial contract may benefit the individual or firm that suspects that their counterparty may engage in an antitrust violation by reducing the expected effort and cost related to punishment if a harmful act is detected. However, the arbitrary nature of the penalty provision entails controversial components from a fairness and justice perspective. For example, a counter-claim was filed in the Kawasaki sewer construction bid-rigging case about an allegedly inappropriately high penalty level for harmful acts, which were set at 20% or 30% of ordered value. An argument used to support this counter-claim was that it was against public order and morality.[15] In its decision regarding this counter-claim, the Court concluded that an assessment of whether a 20% or 30% penalty is so inappropriately high that it violates public order and morality should be based on the size of actual damages. This case illustrates an opportunity for economists to become involved in bid-rigging cases to estimate proper levels of both prospective penalties and damages after the alleged antitrust violation.

Implementing an economic approach to damages involves applying economic expertise to the facts and materials produced in the case, including assessing how economic theory applies to the case and appropriately applying econometric techniques. The prevalence and rigor of quantitative analysis in estimating damages varies across countries, and economic approaches for damages estimation have been utilized in countries where authorities and courts impose fines or damages compensation payments based on damages concepts discussed above.[16] For example, in the US, demand for economic experts in antitrust litigations has grown drastically over the past several decades.[17] Uemura[18] points out that economists' viewpoints on damages estimation have a substantial impact on court decisions in the US antitrust litigation, in contrast to the level of influence economists have in Japan. The difference in involvement of economists in the US versus Japan is visible in both private litigation and government enforcement actions. The Bureau of Economics at the US Federal Trade Commission includes three divisions predominantly staffed with PhD economists[19] and

[15] Murakami, p. 45.
[16] Peter Davis and Eliana Garces, *Quantitative Techniques for Competition and Antitrust Analysis* (2010) p. 347.
[17] Michael R. Baye and Joshua D. Wright, *Is Antitrust Too Complicated for Generalist Judges? The Impact of Economic Complexity and Judicial Training on Appeals,* 15 Journal of Law and Economics 1, 2 (2011).
[18] Koya Uemura, *US Antitrust Law* (2017), p. 106.
[19] Federal Trade Commission, Bureau of Economics Biographies, available at https://www.ftc.gov/about-ftc/bureaus-offices/bureau-economics/biographies (last visited August 12, 2018).

the number of PhD economists in the Antitrust Division of the Department of Justice in the US exceeds 50 as of 2016.[20] By contrast, there were only three PhD economists at the Japan Fair Trade Commission as of April 2018.[21]

To calculate damages, economists use materials specific to the case. In the US, this information is obtained through the formal discovery process, where the defendants, plaintiffs and potentially relevant third parties are asked or compelled to submit data and documents. In addition to performing the damages analysis, economists often work with lawyers in planning and preparing discovery requests, particularly with respect to information that will be useful for estimating damages or making economic arguments. This may be particularly productive in the process of requesting and reviewing data, as the economist may have insight into fields that could be useful in analysis, be able to spot issues with data that might not be as readily identified by lawyers, and pose targeted questions about data.

Methods, arguments, and discovery produced in different jurisdictions may be applicable to analyses relevant to Japanese cases. As discussed above, the concept of the "actual" and "but-for" world can be helpful in estimating damages that are connected to the facts of the case. As a practical matter, firms facing litigation abroad may consider adding parallel Japan-specific analyses to the extent that they may be performing similar analyses in related litigation or for related issues in the US and other jurisdictions, even though stand-alone economic analysis for Japanese cases may seem expensive. Furthermore, even if defendant firms may not go to court in Japan, economic tools to estimate damages are still valuable resources in applications including determining settlement amounts that compensate actual damages, assessments of potential exposure to litigation in other jurisdictions, and addressing fines or penalties imposed by contracts or law.

The application of this framework in Japanese courts may encourage a more scientific approach to assessing damages, which could relate damages awards more closely to the alleged conduct than awards determined by judges without the benefit of economic analysis. Understanding economic approaches to damages could empower courts to better evaluate

[20] Diane S. Owen, *Economists in the Antitrust Division*, CSWEP NEWS (2016), available at https://www.justice.gov/atr/file/economists-in-the-antitrust-division/download, p. 7.
[21] *The Handbook of Competition Economics 2018* (2017), p. 84.

whether plaintiffs really cannot feasibly scientifically determine damages when considering Code of Civil Procedure 248, and, moreover, evaluate damages analyses presented by both plaintiffs and defendants. Furthermore, understanding the role of economists in damages calculations could help plaintiffs, defendants, and jurists work more effectively with economic experts and incorporate damages analyses into their cases.

IV. Conclusion

This paper presents the concept of applying an economic framework to estimate damages, and potential opportunities to and benefits of applying economic approaches to Japanese cases. We hope that Japanese corporations and courts will employ economic tools to estimate damages more widely in the future.