

HARAGUCHI INTERNATIONAL LAW OFFICE

KDX Toranomom Building 9th F,
4-3, Toranomom 1-chome, Minato-ku,
Tokyo 105-0001, JAPAN
Phone: 81(3)6205-4404
Fax: 81(3)6205-4405
E-mail: kharaguchi@haraguchi-law.com

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Kaoru Haraguchi
Founding Attorney
Haraguchi International Law Office
Member of TCM in Japan

Debt Collection and Statute of limitation for Foreign Creditor in Japan

I . Introduction

For more than 15 years, we have been collecting the debts owned by Japanese or Japanese companies on behalf of foreign creditors, previously creditors in US and now those in China. One of the important issues in relation to the debt collection of the foreign creditors in Japan is the statute of limitation of the debts owned by the Japanese debtors to the foreign creditors.

Many of our clients, such as foreign corporations, foreign debt collection agencies and foreign trade insurance corporations often misunderstand that the statute of limitation is governed by the laws of Japan. In fact, the statute of limitation of the debts is often governed by the laws of the foreign creditors, such as the laws of the People's Republic of China.

We discuss the reasons why the foreign law is the governing law of the statute of limitation applicable to the debts to be collected in Japan and some of the important issues associated with the application of the foreign laws, in particular the laws of the People's Republic of China in Japan.

II . Governing Law and the Statute of limitation Period

In case that debtors are located in Japan or incorporated under the laws of Japan, and they have the assets in Japan (which mostly fit to our cases), the convenient way to collect the debts, which is not collectable amicably, would be to file a litigation in Japan and enforce the judgment against the assets of the debtors. In the litigation procedure, the governing law of the statute of limitation of the debts accrued in the international

transaction between the foreign creditors and Japanese debtors shall be determined by the Act on General Rules for Application of Laws (“**Act**”), which is the law regarding the conflict of law in Japan.

With respect to the application of the Act to the issues of the statute of limitation, there is a scholastic opinion claiming that the statute of limitation should be governed by the law of place of the forum, as a matter of procedural law like Common Law system. The prevailing opinion among the scholars and a judgment rendered by the (former) Supreme Court dated March 17, 1917 understand that the legal consequences of the statute of limitation as an extinction of the debts and therefore the governing law shall be decided by the governing law of the debts.

Under the Act, the governing law of the debts is firstly decided by the choice made by the parties of the agreement from which the debt is accrued under Article 7 of the Act, and secondly by laws of the place with which the debts is most closely related at the time of the accrual of the debts in accordance with Article 8(1) of the Act. In case where the special performance, such as the performance of non-monetary obligation is provided by a party to an agreement, the law of the place of the party to the agreement is assumed to be the place most closely related pursuant to Article 8(2) of the Act.

In most of our cases, the foreign creditor is either the seller of the goods manufactured in foreign countries, such as China, thus the law of the People’s Republic of China is the governing law of the debts collected by us from the debtors in Japan.

However, it should be noted that the (former) Supreme Court decision made reservation saying the period of statute of limitation relates to matter of public policy. And Japanese law shall be governing law in case the period of statute of limitation under foreign law is longer than one under Japanese law.

Under Japanese law, the general period of statute of limitation is ten (10) years (Article 167 (1) of Civil Code), five (5) years for commercial claims (Article 522 of Commercial Code), and two (2) years for account receivables of sales of movables.

Contrarily, under Chinese law, the general period of statute of limitation is two (2) years (Article 135 of People's Republic of China Civil Code General Rules), and four (4) years in case of international cargo sales contract.

Because the period of statute of limitation is the double of that under Japanese law, the statute of limitation period of four (4) years as to the international cargo sales under the Chinese Law shall not be applicable to the collection of the debts on behalf of the Chinese creditor in accordance with the (former) Supreme Court judgment.

Of course, there is a criticism alleging that the rule of public policy only applies to cases that the application of foreign law results to contradiction to the Japanese legal order (e.g. applying polygamy in Japan), and the length of statute of limitation shall not be enough. Also, the judgment of the (former) Supreme Court is not binding in Japan and therefore there is a district court decision stating that applying New York law (six (6) years of statute of limitation) shall not violate public policy of Japanese civil law (this case dealt with the statute of limitation of lawyer's legal fee).

We, however, should be careful on the collection of the debts on behalf of the Chinese seller with more than two (2) years because of the risk of the debtor claiming statute of limitation in Japan.

III. Statute of limitation under Chinese Law

1. Outline

Under the law of the People's Republic of China ("**Chinese law**"), there is a relevant law regarding the statute of limitation, which is a counterpart to those under Japanese law.

Under the Chinese law, the creditor would lose the right to collect the debts through litigation procedure if he or she does not collect the debts for certain period. In other words, the creditor would not lose the debts and the collect the debts amicably even after the statute of limitation period elapses (Article 138 of the People's Republic of China Civil Code General Rules).

In China, the Statute of limitation is based on provisions in the "People's Republic of China Civil Code General Rules", and "Provisions of the Supreme People's Court with respect to some problems in applying statute of limitation to proceedings of civil cases" ("**Provisions**") also provides rules of Statute of limitation.

2. Period of Statute of limitation

Period of statute of limitation is 2 years in principle (Article 135 of Civil Code General Rules). In case where it is otherwise provided in other laws, the period shall follow such law (Article 141 of Civil Code General Rules).

Period of statute of limitation in international cargo sales contract is four (4) years (Article 129 of the Contract Act). Therefore, in case where the sale and purchase of the products manufactured in China by a Chinese Seller to the Buyer in Japan, the statute of limitation period for the sales proceed of the products shall be four (4) years.

3. Grounds of Interruption

Statute of limitation shall be interrupted by following events (Article 140 of the Civil Code).

- a. Filing of an action
- b. Demand of one of the parties
- c. Consent by obligators to implement their duty.

In this regard, demand of one of the parties shall include the out-of-court demand, which is different from Japanese law. For example, following acts are accepted (Article 10 of Provisions)

- i) Claim of rights by delivering demand letter
- ii) Claim of rights by posting or transmitting electrical data
- iii) Public notice in case of disappearance of debtors

4. Acknowledgment of debts after completion of Statute of limitation

According to “The Supreme People’s Court: Answer to whether agreement reached between parties on performance of obligations which period of Statute of limitation overran shall be legally protected or not”, in case where the parties agree on performance of obligations after the elapse of statute of limitation, the agreement shall be legally binding. In addition, according to Article 22 of Provisions, in case where the period of statute of limitation elapses and one of the parties manifests his/her intention to agree on the performance of the obligation against the other party, the party may not claim the statute of limitation.

It is, however, not clear as to whether the debtor may not claim the statute of limitation even if he or she admits the debts without the knowledge of the statute of limitation period elapses.

For your reference, this issue was not clear under the laws of Japan. On April 20, 1966, the Supreme Court of Japan decided that the debtor may not claim the statute of limitation even if he or she admits the debts without knowledge of elapse of the statute of limitation period.

IV. Conclusion

It is necessary for us to understand the laws of the statute of limitation of the foreign country where the foreign creditor is located or incorporated where we collect the debts on behalf of the creditor in Japan. It is, however, not always easy to apply the foreign

law of the statute of limitation in Japan as the court of Japan sometimes does not apply the foreign law of the statute of limitation as it is in violation of the public policy of Japan. In case of where the collection of the sales proceed accrued more than two (2) years ago on behalf of the Chinese seller in Japan, it should be cautious to the statute of limitation defense to be claimed by the Japanese debtors.

(Over)