

THE MEDIUM AND SMALL ENTERPRISES IN JAPAN AND THEIR FORMS OF CORPORATION

By EISUKE YOSHINAGA

Professor of Commercial Law and Economic Jurisprudence

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I. The juridical and economic forms of medium and small enterprises

The forms of business corporations are prescribed by the Commercial Law and the *Yugen-kaisha* Law of Japan: the former stipulates the *Gomei-kaisha* (Partnership; *Gomei*=*en nom collectif*; *kaisha*=*société*, company), the *Goshi-kaisha* (Limited Partnership) and the *Kabushiki-kaisha* (Stock Corporation), while the latter the *Yugen-kaisha* (Limited Liability Company, *Yugen*=limited). Legally speaking, the business corporations are joint enterprises with outstanding traits of their own. It must be borne in mind that the Japanese *Gomei-kaisha* (*societe en nom collectif*) and *Goshi-kaisha* (*société en commandite*) are of somewhat different nature from the American Partnership and Limited Partnership respectively although they are both considered as bodies corporate. Amongst other things, it is the form of the enterprise which it takes that determines whether a *Shain* (a partner) or a member of a corporation (an investor) is considered a partner or a member of limited liability, or else a partner or a member of unlimited liability, and it again determines whether a partner's right to his company is a matter of interest or springs from his being a shareholder. Again, while the *Gomei-kaisha* and the *Goshi-kaisha* are a result of the union of personal interests between or among

partners, the *Yugen-kaisha*, although it shares, to a certain extent, the characteristics of the two corporations just mentioned it rather tends to give greater importance to materialistic side. It might also be said that the *Gomei-kaisha* and the *Goshi-kaisha*, being personal unions, place importance to mutual trust more than the *Yugen-kaisha* which emphasizes its materialistic side.

With regard to the choice of the form of corporation, it is left with the enterpriser's private self-determination, who naturally studies the particular traits of the various forms of the corporations in conjunction with its establishment, management and administration, etc. The legislators, however, anticipate that certain types of economic activities will conform with their ideals. Generally speaking, the *Kabushi-kaisha* or a stock corporation is the type of corporation best suited for the working of a big enterprise, while the *Gomei-kaisha* and the *Goshi-kaisha* are the forms of corporation fit for the carrying on a business on a small scale by persons or family members, and lying in between these forms is the *Yugen-kaisha* recognized as a lawful form of corporation and adapted to the operation of small and medium enterprises. The question as to the choice of the form of the corporation which an enterpriser seeks to avail himself of turns on the legality of his business aims and intent which he entertains. Accordingly, it often happens that the small and medium enterprisers prefer the form of *Kabushiki-kaisha* or joint stock corporation, while a gigantic undertaking is not seldom operated in the form of a *Yugengaisha*. Such a state of things suggests itself to the legislators that there might be some sort of problems, juridically or economically, that were beyond their anticipation, it having been shown that there is some discrepancy between the aims and intents of the legislators on the one side and the enterprisers on the other. In other words, various questions present themselves, for instance, how the corporation set forth in the Commercial Law in the abstract is utilized by enterprisers from their view point of economic considerations; whether the juristic form of corporation has harmonized with the economic forms; if there be discord in the economic and jural harmony, how much evil effect and inconveniences are being experienced by the parties concerned; assuming that such is the state of things, whether some measures, economic or juridical, can be discovered to cope with their evil effects.

Although we employ a very comprehensive term 'small and medium' enterprises, it comprises from meagre and petty enterprises to fairly large business undertakings of innumerable shades.

In studying the characteristics of small and medium undertakings with reference to the problems of the commercial law, it is important that attention should be given to the following points:¹

(1) That the enterprise is of small scale. Ordinarily, this fact is shown by the number of the employees. Again the amount of capital is another factor that shows that it is a small undertaking.

(2) In most cases, it is a type of undertaking controlled by one person. This is particularly true in the case of the enterprise of an individual. In this case the prosperity of the undertaking is chiefly due to the initiative of one enterpriser or to the activities of a limited number of persons.

(3) Its household account is not clearly set aside from its business account. In

¹ The data of latest survey.

most cases, the residence and the place of the undertaking are located in the same compounds or area.

(4) It is run or operated by a family or the family's relatives. The portion of labor offered by the family members predominates.

(5) The smaller the scale of the enterprise is, the greater the ownership and management reside in the same individual, obviating the necessity of a third person in the execution of its enterprise.

(6) The small or medium enterprisers are generally more sensitive to worldly customs and profit-seeking than to consciousness of law and right.

(7) They are suffering from excessive competition among the rival enterprisers, the difficulty of financing their enterprise, and taxation, etc. For the solution of their difficulties they no longer are indecisive to resort to legal proceedings.

These itemized seven points just above mentioned are especially noticeable in the case of a very small or meagre enterprise. What I mention in the following chapters refer principally to a small or very small enterprise.

Table 1 The Data of latest survey

Number of employees	Number of enterprises	Ratio against total	Number of family companies	Ratio against total	Number of Kabushiki-kaisha	Ratio against total	Capital per enterprise (1 million yen unit.)
Total & ratio	109,644	100	78,575	72	61,832	56	775
1-3	6,440	5.8	4,833	75	2,209	33	67
4-9	28,720	26.2	21,951	77	10,179	36	65
10-19	34,337	31.3	24,984	73	17,611	52	99
20-29	15,090	13.8	10,716	71	10,205	69	186
30-49	11,629	10.6	8,031	69	8,989	77	199
50-99	7,921	7.2	5,242	61	6,916	87	380
100-199	3,053	2.8	1,836	60	2,839	93	1,013
200-299	972	0.9	520	54	925	95	2,345

"Actual State of Medium and Petty Enterprises." by Teruhiko Iwatake, published June 1959. P. 12.

II. *Forms of corporation preferred by the small or medium enterpriser*

A research might be made as to the reasons why the small and medium enterprisers utilize a form of corporation. It is simply because they expect that the form of a corporation will more or less contribute to the attainment of their object or to the solution of their difficulties they are confronted. The most difficult and embarrassing problem of small and medium enterprisers is how to deal with the question of taxes. Under such circumstances, if they consider that, under the Taxation Law now in force, a corporation reaps better benefit than a private undertaking as far as taxes go, they will

cf. T. Yamanaka. Illogicality in Japanese Small Business. A Survey of Earnings of Small Manufacturing Plants in Japan, Britain and the United States. The Annals of the Hitotsubashi Academy. Vol. X No. 2. p. 142s.

not hesitate to proceed to incorporate their undertakings quite naturally from their calculating nature. Such attitude is nothing but the fact that they are motivated by their profit-seeking desire. It must be remembered that the corporation prescribed in the Commerce Law was not created for such purposes as reducing taxes. Aside from the question of their motive, once an undertaking has chosen a jural form of corporation it must observe and be subjected to the stringent provisions of the law irrespective of its desire or dislike. And in the case of the compulsory provisions the breach of which will subject the enterpriser to a liability or a nullity as the case may be. In proportion to the degree of the presence of compulsory provisions, the law is often said to be "stiff" or "tolerant". It does not necessarily follow that these "stiff" provisions always work a detriment to small or medium enterprisers. On the contrary, it may be said that by being a juristic person, for instance, a *Yugen-kaisha* or a *Kabushiki-kaisha* (stock corporation), a small or medium enterprise may enjoy greater development or rationalization which it eagerly desires.

Let me proceed to the discussion on the problem of the effects that accrue to a small or medium undertaking from its being incorporated. I shall endeavor briefly to enumerate them summarily.

(1) In case a private enterprise is incorporated into a *Kabushiki-kaisha* or a *Yugen-kaisha*, the unlimited liability of the individual members becomes a limited one, the *Shain* (a partner) undergoing change in his status from a partner to a stockholder.

(2) A corporation being an independent body corporate, it is qualified to own assets of its own. Where the assets of the corporation correspond with its business assets the line of demarcation can clearly be drawn between household accounts and business accounts, establishing thereby a rationality of the working of its capital.

(3) The form of stock or *Mochibun* (Interest) makes it possible to make joint or common investment, which tends to create prospect for the increase of capital of its own.

(4) The compulsory provisions for the preparation of accounting statements lead to rationalization of management and the fairness in bearing taxes.

(5) The family labor can be appraised justly.

(6) The death or change in individual membership will not affect the continuity of the enterprise.

III. Preference: *Kabushiki-kaisha* or *Yugen-kaisha*

The purpose of legalizing a corporation is not merely to enable the enterpriser to utilize the juristic form, but it aims at protecting the rights and interests of the third parties, especially of the creditors, the consequence of which will also tend to a healthy maintenance of the enterprise. It naturally follows that the strict observance of compulsory provisions of the law is demanded of the corporation so long as it is a corporation, whatever the intention or desire of small or medium enterprisers may be, in resorting to that form of juristic person. These compulsory provisions are concerned with the adjustment of the interest of the persons concerned, and particularly with the protection of the interest of creditors and the security of transaction in general.

The minimum of the demand of the compulsory provisions on the corporation is not uniform for various forms of corporations. Again, these provisions are not necessarily carried out as a matter of fact in certain cases of economic conditions. It is needless to say that the corporation, whether of small or medium scale, should observe the laws, but whence or wherein come or rest the reasons or causes that the observance of the laws is sometimes neglected? In the first place this comes from the enterpriser's selfish, calculating idea. He wishes to avoid all formal proceedings and tries to evade the formality required by laws. Thus, for any burden incurring on him expenses and labor he makes his best he can to minimize it. To make the matter worse, some go so far as to disregard or do away with all cumbersome or troublesome procedures, and the result is that they are subjected to a censure for illegality as well as for disregarding the spirit of the law. In the second place, such disregard of the legal provisions comes from the fact that their character is the reflection of *Gemeinschaft*. Their individual consciousness of right as well as the compulsory acceptance of legal system of *Gesellschaft* often are the causes of their repulsion and abomination against strict observance of the provisions of the law. The result of the conjoint working of the two circumstances just mentioned is that the small and medium enterprise corporations have not so far satisfied the expectations of the law. On the other hand, however, the features of advantages and disadvantages of juridical persons have not been fully made use of. Generally speaking, taking into consideration the inconsistent elements of these juristic persons, it may fairly be said that the *Yugen-kaisha* is the most suitable type of corporation. In other words, the *Yugen-kaisha* is simpler and more elastic in its legal forms and procedures than other forms of corporation, and it might be considered that it is most suited to the small and medium undertaking.

However, there are a fairly large number of medium and small enterprises that are operated under the *Kabushiki-kaisha* system. Such corporations have been prompted to adopt the *Kabushiki-kaisha* system from various reasons. It was the first of January 1940 that the *Yugen-kaisha* Law (Limited Liability Company Law) went into effect, and the *Kabushiki-kaisha* was the only form of corporation till then that enjoyed limited liability together with the right to limit the transfer of stock. Even after the enforcement of the *Yugen-kaisha* Law, the enterprisers tended to avoid incorporating the term *Yugen-kaisha* in its trade name, it being considered as of less value as its good will than *Kabushiki-kaisha*.²

However, by virtue of the revision of the Commercial Law in 1950, it gradually came to be confirmed that the *Kabushi-kaisha* is the type of the legal person most suited for carrying on a business on a large scale. The *Yugen-kaisha*, on the other hand, by its diffusion and enlightenment of the public, gradually has come to be considered a system most appropriate to the management of small and medium enterprises. This trend is

² Some medium and small enterprisers have an erroneous concept that by employing the trade or firm name of *Kabushiki-kaisha* they can impress on the public with a greater scale of business or trade than they actually deserve. Reversely, the trade name of *Yugen-kaisha*, they think, connotes smallness of everything connected with the enterprise, its liability, its number of employees, even its future development and prosperity. Even such nonsensical assumptions are not to be disposed of as a mere laughing stock by the enterprisers who are oppressed by severe competition from their rival enterprisers and always exposed to their business adversity.

shown in the statistics.³

IV. *Incorporation of a private undertaking*

The transformation of a private enterprise that has hitherto been a medium or a small enterprise to an incorporated enterprise is undoubtedly a subject that deserves some close attention. Outwardly, in most cases, the Commercial Law nomenclature, the *Kabushiki-kaisha* or *Yugen-kaisha* is prefixed or added to the trade or business title joined with the personal name of the enterpriser, for instance, *Kabushiki-kaisha John Doe Ironworks* or *Yugen-kaisha John Doe Ironworks*; *Kabushiki-kaisha John Jones Shoten* (Store) or *Yugen-kaisha John Jones Shoten*. (The Commercial Law Art. 17.) However, it must be considered that here a great change is being worked intrinsically and inwardly, to wit, the enterpriser has come to own his assets in the company, entirely different from the assets of the individual investor, an entirely independent new personality having been created. It is, in the first place, with reference to the corporation in which the personal name of the enterpriser is part of the trade or firm name. In the second place, it is with reference to the relation between the former trade owner who had hitherto had a sole control of the trade and the newly established corporation. This former trade owner ordinarily has control over the greater or major part of interest or the stock of the newly formed corporation.

(1) Trade or Firm name.

In the case of personal or individual undertakings, a person may freely employ his or her surname or family name as well as his or her full name as part of the trade name. (The Commercial Law, Art. 16.) A large number of small and medium enterprisers customarily employ their surname or full name in their corporate names. To employ his surname or full name in his corporate name is beneficial to the enterpriser as it has the advantages of showing to the public his credit or trust as well as his willingness to meet all claims and liabilities. In so far as the enterprise is a personal undertaking, his liability, it is needless to say, is unlimited. It may be said that he employs his surname or full name to show to the public that he is the person responsible to all liabilities. In France, the legislation makes it compulsory to indicate the enterpriser's personal name in its trade name of the *Gomei-kaisha* (*Société en nom collectif*), and this may be attributed to the same reason. In Japan, too, I do not say that such provision to that effect is absent in our Commercial Code. To give an illustration, where the trade name of a *Gomei-kaisha* contains the surname or full name of the retired *Shain* or partner, such retired *Shain* or partner may ask the remaining partner or partners not to use his surname or full name by the *Gomei-kaisha*. The purport of this provision is to protect the retired *Shain* or partner from being made responsible from the mere fact of his name appearing as part of the trade name. (The Commercial Code, Art. 92. cf. also. Art 83.)

The principle shown in the provisions controlling the *Gomei-kaisha* that the person

³ "Actual State of Medium and Petty Technical Industries." By Akihiko Iwatake, published June 1959. This is an authoritative and painstaking work furnishing a good deal of materials for the present thesis.

whose surname or full name is part of the trade name of the *Gomei-kaisha* shall take full or unlimited liability is left out of consideration in the case of *Kabushiki-kaisha* and the *Yugen-kaisha*. To use a concrete example, in the case of the *Gomei-kaisha* if the undertaking went by the firm name of *Gomei-kaisha John Doe*, this said John Doe, even if he was not as a matter of fact a *Shain* or partner, he would be made liable, for having misled the third party even due to the third party's misapprehension. In the case of the *Kabushiki-kaisha John Doe*, this John Doe's liability will not be unlimited even when the third party firmly believed, due to his misapprehension, that he is. This difference of liability has led to an evil effect in the case of medium or small enterprises. This often happens in the case when John Doe makes a dealing or transaction. Question arises as to whether John Doe made the dealing or transaction in the capacity of the president of the *Kabushiki-kaisha* or else he conducted himself in the capacity of an individual person. There is abundant room for doubt and obscurity, especially at the inception of the formation of the *Kabushiki-kaisha*. Again, even when an agreement is made in writing, it often happens that the other contracting party is unaware that he is dealing with the *Kabushiki-kaisha*. The persons who are not conversant with legal knowledge enter into agreement, placing personal trust on the person he deals with, not knowing that he is contracting with the *Kabushiki-kaisha* or *Yugen-kaisha*. In certain cases, it is only the *Kabushiki-kaisha* that becomes the subject of rights and liabilities, and no claim can be laid against the former enterpriser or *Shain* (partner) after its incorporation. Of course, if the *Kabushiki-kaisha* is solvent and able to meet claims there is nothing to worry about, but there may be cases where the *Kabushiki-kaisha* turns out to be propertyless and unable to meet claims. For instance, the store or factory is apparently owned by the *Kabushiki-kaisha*, but it turns out that it was rented, and that much of its working capital was a loan. In this case, even if the loan was made to the enterpriser prior to the establishment of the *Kabushiki-kaisha* the person who made the loan cannot make claim against the borrower directly to him, his legal personality having undergone change. Should the *Yugen-kaisha* be made such a wrongful use of, the person concerned with it would be subjected to a reproach that it is in Germany *Gesellschaft mit bösen Hintergedanken* or the corporation with malicious intentions.

In order to protect creditors from evil practices thus far mentioned the law should provide the minimum amount of capital for the *Kabushiki-kaisha* and the *Yugen-kaisha* sufficient for the purpose. When an enterprise is incorporated, on its establishment, in conformity with the provisions of the law, it should possess assets corresponding to its capital, and this will give proper protection to creditors. However, it is with regret that there is no provision in Japan regulating the minimum amount of capital with respect to the *Kabushiki-kaisha*. There is a provision, it is true, pertaining to the minimum amount of capital in the case of the *Yugen-kaisha* (The *Yugen-kaisha* Law. Art. 9.). But the amount prescribed there being one hundred thousand yen (Y100,000) is far from being sufficient for affording proper protection to creditors, and it is desired that some legislative measures should be taken speedily.

(2) Incorporation is not recognized as a profit-seeking means, but it is to establish fiduciary obligations.

In the world of small and medium enterprises, the prevailing condition is that an

efficient and able enterprisers coexists with or located side by side with juristic persons or corporations. This is shown statistically from the fact that regionally overwhelming number of enterprisers have their dwellinghouses and their places of business in the same locality.⁴

Herein lies the source of the problem that springs from this relation. The efficient and able enterpriser is originally the president or director of his enterprise, and as such his fiduciary obligation is of great importance in the small or medium enterprise how much his obligation is fulfilled.

Both the *Kabushiki-kaisha* and the *Yugen-kaisha* place, it is needless to say, their fiduciary obligations on the directors (The Commercial Law. Art. 254; The *Yugen-kaisha* Law Art. 32.) The director as such should make his greatest efforts in the interest of the corporation, and he should on no account have his hand in dealings that bring or result in the profit to himself or to a third party, agasinst or at the sacrifice of the interest of the company. This is a matter of course viewed from the nature of the enterprise, but a reverse effect is sometimes noted in the small and medium enterprises. There are, it is said, cases in which the interest of the corporation is subordinated to the interest of personal gains. Where the scale of the corporation is the smaller, the greater is the degree of a wilful use of the company assets, taking advantage of its stricture. This tendency is especially conspicuous in the 'one man' company of an efficient and able enterpriser. The ideal concept of the commercial law demands that if such a state of things prevails, in addition to the duties of a good custodian, more stringent fiduciary obligations should be taxed.

In view of the fact, however, in small and medium enterprises, the management of a company is at the same time his profession and the means of sustenance of his household, and his being faithful to the execution of his fiduciary obligation will concurrently be his ardent management and operation of his trade, even though an emphasis is not laid on his fiduciary obligation. It might be considered that such is a special feature of the small and medium enterprises where ideals of enterprise are smoothly carried out. In short, the sincere and faithful enterprisers of small and medium scale will pursue the former course in most cases, although it cannot be assured that there never are those who make instrumentality of incorporation for their selfish purposes. For the prevention of such underhanded designs, an emphasis on greater fiduciary obligations and the raising of the standard of economic morality would subserve to that purpose.

(3) Capital

As a rule, money is ordinarily the form of contribution to be paid by the *Shain* at the time of the establishment of the *Kabushiki-kaisha* or the *Yugen-kaisha*. Although con-

Number of persons employed	Enterprise account divided from household accounts	Dwellings in same area of enterprises
Total average	45.7	85.5
1-19 persons	41.5	87.3
20-49 persons	42.1	71.4

"Statistics Showing Actual State of Medium & Small Enterprises." By Teruhiko Iwatake. Published June 1959. P. 49.

⁴ The division of enterprise accounts from household accounts.

tribution in forms of property other than money is sometimes made, it is subjected to rigorous restrictions as it accompanies a good deal of danger from this anomalous way of investment. The same principles apply to the property which has been stipulated to be taken over after the coming of the company into existence. The law requires that the *Kabushiki-kaisha* or the *Yugen-kaisha* should make detailed provisions as to the investment in kind and the underwriting of property in its articles of incorporation. Furthermore, the *Kabushiki-kaisha* must have an inspector appointed by proper court of justice who will adjudge on the assessment of its property. Again, in the case of the *Yugen-kaisha*, over assessment of its assets compels the entire members of the *Yugen-kaisha* at the time of its establishment to supplement or replete the assets in a very stringent wording. (The *Yugen-kaisha* Law. Art. 14.)

Where a medium or small enterprise has been incorporated, and investment in kind and underwriting of property constitute a greater portion of its assets, it is questionable how much and how far the stringent provisions of the law have been observed. In the case of the *Kabushiki-kaisha*, if it were to try to avoid the application of the strict provisions of the law, the promoters may establish a company by investing money nominally. Assume that seven promoters underwrite five hundred yen face value share each, the consequence would be that they secure a sufficient amount of three thousand and five hundred Yen capital. These promoters will endeavor to procure operating assets or renting a workshop, etc. being unable to keep their firms going with their limited capital. Such will naturally work evil effect by injuring the interest of the creditors. In the case of the *Yugen-kaisha*, instead of the assessment by the inspector appointed by the court, any overassessment of its assets is to be supplemented, but it is doubtful whether or not the provisions of the law are carried out to the letter, particularly in the case of a family partnership, for giving sufficient protection to creditors. A far more important question arises in drawing a clearcut line of demarcation between the company assets and the assets of its *Shain* or a member of the company. What was generally assumed to be the assets of the company it often turns out that they are the assets of its individual member, or *vice versa*. In the case of a *Gomei-kaisha* or a partnership a clear line is drawn, and the amount contributed by each *Shain* or partner is accurately ascertainable from the records at the Registration Office. (The Commercial Law. Art. 64, item 1, sub-item 4.)

Contrary to the case of a *Gomei-kaisha*, the matter is stated only in the Articles of Incorporation in the case of the *Kabushiki-kaisha* and the *Yugen-kaisha*. Moreover, such statement in the Articles of Incorporation is generally deleted at the following stockholders' or partners' general meeting. Consequently, there is absolutely no provision stipulating the distinction of private assets from those of the company, and it might be said that the protection of the creditors is, in the case of small and medium enterprises, smaller than in other types of companies.

I have shown before that in the small and medium enterprises there is no precise standard of distinguishing private assets from company assets, and that the making of public notices of the firm assets constitute an important solution of the problem. For the solution of this problem, it may be proposed that the compulsory publication of the inventory or Financial Statement with detailed statements should be required. Another measure for this purpose would be to fix the minimum amount of capital at

quite a high figure as I have stated in connection with the trade name. Under the present circumstances it may be considered that the minimum amount of capital should not be less than five million yen (¥5,000,000.) in the case of a *Yugen-kaisha* and fifty million yen (¥50,000,000.) in the case of a *Kabushiki-kaisha*.

V. *Management of the business corporation*

(1) Is the stockholders' meeting actually held?

So long as the *Kabushiki-kaisha* and the *Yugen-kaisha* are juridical persons, they must call a stockholders' meeting or a partners' meeting respectively at a certain occasion stipulated in the Articles of Incorporation (The Commercial Law. Art. 234; the *Yugengaisha* Law. Art. 41.) These general meetings greatly differ in their character. In the case of the *Kabushiki-kaisha*, association spirit or *Gesellschaft* is reflected in all its procedures; the calling of a meeting, the manner of proceeding, the taking of votes and reaching a resolution, are all governed by stringent rules. In the case of the *Yugen-kaisha*, the smallness of scale and *Gemeinschaft* or comradeship are reflected, the rules of governing the holding of meetings being greatly relaxed. To illustrate this, in the case of the *Yugen-kaisha*, a person may legitimately participate in its resolution in writing, which is not recognized in the case of the *Kabushiki-kaisha*. Again, the resolution passed by the meeting which was attended by the entire members without notice in due process has been diversely interpreted in the case of the *Kabushiki-kaisha* is made lawful by an express provision in the law of the *Yugen-kaisha*. In view of such state of things, therefore, to incorporate a small or medium enterprise by going through a complex procedure would be a mere waste of time and expenses. Primarily the medium or small enterpriser is most eager to minimize its expenses and moves always after profits, and it is difficult to understand why he desires to transform his private undertaking into a juristic person. It is said that the matter is cleverly dispensed with. I am told that all requirements of the law being met by preparing documents with the use of a seal impression. It is needless to say that such perfunctory management of the *Kabushiki-kaisha* as drawing up necessary papers will not satisfy the provisions of the Commercial Law. The shareholders' meeting or the directors' meeting which has not actually been held is nonexistent so far as the Commercial Law goes and is therefore utterly devoid of its effect. When the authorities come to cognizance of such a state of things a severe sanction will be inflicted and the company come to suffer disadvantages. From this state of fact just mentioned, it is quite certain that the *Yugen-kaisha* in which the resolution in writing is given its full effect and also the general meeting without due notice attended by all members is likewise of legal validity is better adapted to a medium or small enterprise than the *Kabushiki-kaisha*. In spite of such facts, the number of small enterprises taking the form of a juridical person still continues to augment, and this may be attributed to the shallowness of legal knowledge on the part of the enterprisers or else the semblance of the *Yugen-kaisha* and the *Kabushiki-kaisha*, not only as a matter of form but also concretely, seems to appeal to such enterprisers. (In extreme cases there are corporations sole, practically.)

(2) Is accounting properly conducted?

(a) Dividend distribution.

In the medium or the small enterprise in which a clear dividing line is not drawn between its business and household accounts and, moreover, where the household account plays its major role over the business account, the method of dividend distribution is naturally different from that of other types of enterprise. Profit is nothing other than the legal fruit which capital has produced, and the dividend distributed is nothing else than the price of compensation for the efficient use of the capital. Consequently it may be said that the amount of profit is to be decided in proportion to the working or the use of the capital, and the profit that accrued to the enterprise is the basic amount of the dividend distribution. Where household accounts, however, have preference over the enterprise accounts of the small or medium undertaking, the distribution of dividend must be conducted when there is surplus after the payments of household expenses. In order to make dividends, however, no confusion of household accounts with business accounts being permissible capital must be very efficiently employed. If that could be done there would arise no difficulties, but if there be no profit to be divided then difficulties crop up. Just as the *Kabushiki-kaisha*, the *Yugen-kaisha* too is prohibited from making a bogus dividend in rigid terms. (The Commercial Law. Art. 290; *Yugen-kaisha* Law. Art. 46.) On the side of the enterpriser himself and his family, the expenses to maintain his household must be met by all means. In the case of the *Gomei-kaisha*, the fundamental principle of the maintenance of capital has been abandoned and the dividend is permitted even when its account is in the red, priority being given to assuring household accounts. For the *Yugen-kaisha* no dividend is recognized when its account is in the red, considering the necessity of maintaining capital. In the medium and small enterprises, in order to evade the stipulation of the law two methods may probably be resorted to: first, by contriving to show its profit on the face of its financial statements; secondly, payments being made in the form of allowances or compensations to the directors and auditors or to the family members for their labor; As regards the tampering with the accounting documents, it may be said that, up to four or five years ago, only a comparatively small number of small or medium enterprisers have well established their accounting book system, and even at the present time, there are not many whose account books are perfect in all respects. It is also said that different financial statements are tendered to the tax offices and to the bank with which the enterpriser has dealings. For the *Yugen-kaisha*, the law does not demand that its account documents should be inspected by the certified public accountant or be certified by the auditor, and this fact makes tampering with the account documents a matter of facility. So long as the account book system is not firmly established in the small or medium enterprises, bogus dividend would be made possible however much the provisions were stringently enforced on the *Kabushiki-kaisha* to have its books audited by its certified public accountant. There is, of course, a provision prescribing the refunding of the amount of bogus dividend. (The Commercial Law. Art. 290, para. 2.) In this way, creditors are often without proper protection, the provision of refunding the amount of bogus dividend being a matter of impracticality.

These studies conclusively show that the establishment of the account book system endorsed by the truthfulness of accounts is the question to which priority should be given in order to solve the problem. In connection with the small or medium enterprise it

may be said that the establishment of a perfect accounting system, along with the legal enforcement of the provisions prescribed by the law, is beneficial to those who are concerned with the enterprise as well as to the tax offices. This makes it imperative that the enterprisers themselves should be made to realize the necessity of their conforming to such measures. To the profit and loss statement of a large undertaking should be attached much importance, and likewise in the case of a small or medium enterprise importance should be laid on the inventory in which investment in kind is publicized with the detailed statements attached. The provisions should be made with reference to the method and manner of publicizing its financial papers and documents.

(b) Compensation and salary.

The compensations to be paid to the officers of the company and the wages to be paid to the workers are a part of operating expenditure to be dispensed with as such. This amount of expenses, irrespective of its loss or profit, may be defrayed to those who are entitled to the same. In the medium or small enterprise that depends on the labor of the family or that of 'one man', the payments will likewise be made in order to maintain the household. Such amount of defrayal or the regulations concerning the same will be determined by the 'one man' or by the family. In distributing its profit no one will object to its decision where no or nearly no outsiders are investors, even if it went so far as to sacrifice its dividend distribution, impairing thereby the interest of its creditors. This is because the enterpriser will enter in the books as payments for family labor under unpaid debts account which enjoys priority to that of the creditor, or such claims will, at least, concur with that of the creditor.

(c) Mitigation of the principle of the maintenance of capital.

(Grundsatz der Bindung des Grundkapitals, règle de la fixe, ou l'intangibilité du capital social)

From the legislative point of view, the question to what extent the capital should be maintained and the problem of the mitigation of capital maintenance might be considered in view of the fact that the *Yugen-kaisha* is a personal union in its character. In other words, mere upkeep of its capital will suffice, and the establishment of the legal reserve is, from a legislative point of view, only for replenishing its loss or applying it to dividend distribution. In that case, however, it would be necessary that the law should provide that the investor should make additional investments. To the small or medium investors who are subjected to ever changing ups and downs of the market such measures might be the most suited to them.

(d) Liabilities.

For fund raising by borrowing, the *Kabushiki-kaisha* enjoys much more convenience than the *Yugen-kaisha*, because the *Kabushiki-kaisha* is entitled under the law to issue bonds or debentures, while it is commonly held that such is not the case with the *Yugen-kaisha*. The fact is that most small or medium enterprisers are financially embarrassed, and the petty enterpriser is quite unable to borrow his operating fund. In some cases there is no lender at all. The issue of company debenture is entirely out of the question. Now then, what is the possible mode of securing a loan for him? In the small or medium enterprise, as has been detailed elsewhere, the enterpriser and the company are located in the same compounds. Although the company is responsible, as a matter of form, as a separate entity, economically speaking, its personality is merged with that of the

enterpriser or the efficient controller of the company. Such being the case, in most cases borrowings are made as joint debts of the company as debtor in name and the efficient enterpriser (the president) in his name as enterpriser. It often happens that some efficient *Shain* or partners or some member or members of the family may join as joint debtors. The reason for taking such procedure may be explained by the fact that the business assets, which were originally an undivided whole, were divided into two by its being incorporated; that the credit or the assets of the efficient member of the company are of greater value than those of the company; that the participation of the family members will enhance the value of the security, they being joint debtors.

There would almost be no difference when the debtor company is engaged in individual undertaking if such a procedure followed, and in so far as the creditor is concerned his rights will practically be the same as in the case of the *Gomei-kaisha* in which the *Shain* or partners will be of the unlimited liability. After all, in this case the results would be entirely the same as in the case of the *Gomei-kaisha* and moreover it may be said that the unlimited liability of the *Shain* is united with the company's liability. It is needless to say that the interest of the creditor is more firmly protected than in most other cases. If such a form be adopted by all the enterprisers, the *Gomei-kaisha* and the *Goshi-kaisha* would be considered the most appropriate forms.

VI. Conclusion

Thus far I have expressed my views on the forms of small and medium enterprises, and especially have dealt with the questionable points in connection with the *Kabushiki-kaisha* and the *Yugen-kaisha* which are widely made use of by the enterprisers.

From the standpoint of a jurist, it may be said that the ideal form for medium or small enterprise is either the *Gomei-kaisha* or the *Goshi-kaisha*. The incorporation of the personal name in the trade name is preferred to leaving his personal name of the enterpriser unexpressed. And why is it that the *Gomei-kaisha* or the *Goshi-kaisha* does not appeal to enterprisers but is avoided or disliked, in certain cases, preference being given to the *Kabushiki-kaisha* or *Yugen-kaisha* against the intent and purpose of legislation? The primary inducement is that the latter offers greater freedom or convenience to the enterpriser: he, a private individual by becoming a shareholder of a company, secures personally a legally irresponsible position; he harbors an intention to keep separate his assets of his own intact in time of business slump, the risk being borne by the specific assets of the company. In the second place, the prevalence of the worship of economic power among the enterprisers of small and medium enterprises has contributed not a little towards adopting the *Kabushiki-kaisha* by which these enterprisers seek to 'water' their assets and show off that they are doing a greater business than actually are; in the third place, they are prompted from a consideration of the tax laws. The Tax Laws deem most small and medium undertakings as family companies, but it is not clear in this respect whether the *Kabushiki-kaisha* enjoys more favorable treatment than the *Yugen-kaisha* in the law. The *Kabushiki-kaisha* is open and public in its nature and is inconsistent with the family company in this point, and where it is dubious as to whether an enterprise is a family undertaking or not, it will serve psycho-

logically for negating the existence of a family company.

It is, after all, my conclusive belief that it is neither the *Gomei-kaisha* nor the *Kabushiki-kaisha* that is most suitable or beneficial to medium and small enterprises, but it is the *Yugen-kaisha*. It can enjoy legal as well as economic privileges from its being an organization of exclusive nature, its simplicity of structure, management, operation with less labor and expenditures. It must be borne in mind that the law should not neglect affording protection to creditors. In order to properly protect creditors, as I have previously mentioned, it is imperative that the following measures should be provided in the law. First of all, the minimum amount of capital should be raised. For instance, if the amount of capital of the *Yugen-kaisha* were to be raised to five million yen, other lesser enterprisers who fail to come up to that standard of amount should be made a *Gomei-kaisha* or a *Goshi-kaisha*. In this case, personal name might be allowed in the trade name only when he is a member of unlimited liability of that firm. Secondly, some measures should be provided by which the distinction of enterprise assets from personal assets is made clear by publication. Thirdly, for the *Kabushiki-kaisha*, too, a far higher amount of capital should be fixed as a minimum, say, fifty million yen.

The *Kabushiki-kaisha* is nevertheless without its advantages, but it involves much labor and expenses that reduce such advantages. Any efforts to reduce such disadvantages will cause illegality of some sort. The medium and small enterprises, as economic forms, are presently suffering from the complexity of procedures which the enterprisers had never anticipated. Of the medium or small undertakings that entertain a future development into a gigantic enterprise or a publicized corporation, the form of a *Kabushiki-kaisha* might be recommended as an exception.

From the considerations thus far made, the transformation or reorganization from the *Kabushiki-kaisha* to a *Yugen-kaisha*, or *vice versa*, should be carried out smoothly as much as possible, it is hoped, paying a good deal of attention to the character and growth of the enterprise. In the former case, its transformation is possible by a unanimous vote of the shareholders at its general meeting, provided that the debentures of the corporation have all been amortised. Such transformation or reorganization in the latter case will be legally ineffective without the authorization of the court of justice. (The Law of *Yugengaisha*. Art. 60, 64.) Even such a trifling affair is viewed by the medium or small enterpriser as troublesome affair as he is apt to judge things from his calculating view point. It may be said that the inconsistent state of affairs between the economic forms and the legal forms for medium and small enterprises is likely to continue in the future for an indefinite period of time. Another measure for inviting the change from the *Kabushiki-kaisha* to the *Yugen-kaisha* is to reduce the tax on such *Kabushiki-kaisha* that will undertake such change. The policy will no doubt encourage to make reorganization of the petty and medium enterprisers who are generally of calculating nature.

(Jan. 7, 1960)