

What to know about internal reporting systems in Japan

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In brief

- According to a survey by the Consumer Affairs Agency, corporate misconduct is most commonly detected through internal reporting. The most common reports are of harmful behaviours at workplaces such as abuse of power or sexual harassment.
- The amended Japanese Whistleblower Protection Act requires business operators to create a system for responding to whistleblowing reports. Small and medium sized business operators with 300 or fewer employees are obligated to make a 'best effort'.
- An effective internal reporting system requires certain functions that include employee peace of mind and the ease of access when reporting, as well as the ability for the person handling the reports to respond and manage them efficiently.

In detail

1. What is an internal reporting system?

In many instances, cases of corporate misconduct are brought to light by reports from an employee within the company. In a 2016 survey by the Japanese Consumer Affairs Agency, the largest number of respondents, at 58.8%, cited internal reporting by employees (through means such as internal reporting systems and direct reporting to management) as the most common means by which corporate misconduct is discovered.

An internal reporting system is a means of receiving internal reports of misconduct from employees and protecting whistleblowers who report an incident as well as a means for business operators to conduct appropriate investigations and set forth corrective and preventative measures in relation to a given complaint.

(1) The significance of an internal reporting system

According to the Guidelines for Private Enterprises Regarding the Development and Operation of Internal Reporting Systems Based on the Whistleblower Protection Act, the introduction, maintenance and operation of an effective internal reporting system by a business operator improves an organisation's self-cleansing function and contributes to the promotion of compliance management. It also leads to improvement of the corporate values and sustainable development of the organisation by gaining the trust of stakeholders such as consumers, trading partners, employees, shareholders, investors, lenders and the local community.

In addition, business operators who provide safe and high quality products and services through risk management that makes proactive use of an internal reporting system play an important role in terms of securing the interests of society and the economy as a whole, and fulfilling their corporate social responsibility.

(2) Common example of reporting

According to the aforementioned survey, the most common types of reports that are submitted to internal reporting systems are reports of abusive behaviours at workplaces, such as abuse of power or sexual harassment (55%), followed by reports of concerns that are not necessarily misconduct, such as personal issues with other employees (28.3%), and violations of company rules (27.5%).

The most common challenge that business operators face when operating their internal reporting systems is that these systems are used by employees to report issues that are not misconduct, but simply complaints or dissatisfaction with the workplace (35.7%). It is true that the more employees are aware of the existence of the internal reporting system, the more such complaints will be reported. Nevertheless, in order to ensure the internal reporting system operates effectively, the first step to take is to create an easy-to-use environment and raise employee awareness. In addition, employees need to be informed of the types of incidents that should be reported through training and internal publicity.

2. Amendment to the Japanese Whistleblower Protection Act

The original Whistleblower Protection Act was passed in 2006. However, corporate misconduct continues to occur, and we frequently see top management apologising to the public via mass media. If these companies had had effective internal reporting systems and handled the problems appropriately at an early stage, the outcomes may have been different. In response to the necessity of preventing damages through the early detection and correction of corporate misconduct, an amended Act was promulgated on 12 June 2020 with the following major changes. The amended Act will take effect within two years from the date of promulgation.

(1) Facilitate internal reporting by whistleblowers and correction of misconduct by business operators

Under the amended Act, business operators are obligated to create a system for responding to whistleblowing reports, including establishing internal reporting channels and measures for investigation and correcting misconduct. Small and medium sized business operators with 300 or fewer employees are obligated to make a 'best effort'.

In order to ensure the effectiveness of the above obligations, the amended Act introduces administrative measures such as providing advice, guidance or recommendations to business operators. If the business operator does not follow such administrative recommendations, the company name could be publicised.

Under the amended Act, persons in charge of handling whistleblowing reports are obligated to protect the confidentiality and identity of the whistleblower. If such a person violates this obligation, they could be subject to criminal penalty charges.

(2) Facilitate reporting to administrative agencies

The amended Act relaxes conditions for the protection of a whistleblower who submits a report to an administrative agency. Under the current Act, the whistleblower cannot legally be dismissed if they have 'reasonable grounds to believe' that the reportable offence has occurred or is about to occur. However, it is difficult for ordinary people to determine or prove that there are reasonable grounds to believe that the reported allegation is in fact true. Under the amended Act, this requirement is relaxed, and the whistleblower is protected as long as they believe that the reported offence has occurred or is about to occur, and that they provide certain information in writing such as their full name, address and details of the reportable fact. Moreover, the amended Act obligates administrative agencies to establish a system for responding to whistleblowing.

Similarly, the conditions for the protection of a whistleblower who reports misconduct to the news media and other external parties are also relaxed.

(3) Ensure the protection of whistleblowers

Under the current Act, the term 'whistleblower' is defined as a current employee who reports an incident or makes an allegation. The amended Act expands the definition of a whistleblower to include executives and former employees (as long as they make a report within one year after resignation or retirement).

The amended Act also expands the scope of whistleblowing. Under the current Act, the term 'reportable fact' refers only to conduct that is subject to criminal punishment. The amended Act expands this definition to include conduct that is subject to administrative sanctions.

The current Act does not have any clause to limit the compensation rights of business operators. However, the amended Act prohibits business operators from claiming compensation against a whistleblower for damages incurred by the whistleblowing report.

3. Effective internal reporting system

Internal reporting can be performed via various means, such as telephone, e-mail, and the internet. When a business operator introduces a new internal reporting system or makes improvements to an existing one, the system needs to be equipped with certain functions that ensure the employees' peace of mind and ease of access when reporting, as well as the ability for the person in charge of handling the reports to respond and manage them efficiently.

(1) Usability

An internal reporting system needs to be easy to understand and use, and should make it easy to communicate and gather information. An anonymous reporting option should be available if a whistleblower desires to hide their identity. Even if the report is submitted anonymously, means for interactive communication between the whistleblower and the person in charge should be implemented.

(2) Agility

Whistleblowers often have an urgent need to report an incident or allegation when they witness misconduct or wrongdoing. Therefore, an internal reporting system should be able to be accessed anytime, from anywhere. Fast technology enables users to submit reports through various means such as a PC, smartphone or tablet 24 hours a day, 365 days a year.

(3) Security

In order to protect the confidentiality of whistleblowers, reports need to be received in a secure environment. If the person in charge of handling the reports works within the office, appropriate measures must be taken such as meeting the whistleblower in an isolated room, outside the office, and/or after the business hours, as well as taking other means to ensure the protection of the whistleblower. Moreover, if reports are managed as digital data, personal information needs to be protected through access control, system vulnerability checks and access log retention.

(4) Global use

When a business operator implements an internal reporting system for its overseas subsidiaries, it needs to provide local language support. And the collection of personal data and transfer of such data outside the territory is subject to local personal data protection and labour laws. It is therefore essential to check the territory requirements and handle the relevant data in accordance with those requirements.

PwC's Internal Reporting Platform is a cloud-based, multilingual service that provides an efficient and effective system for rapidly responding to whistleblowing reports on a global level. The PwC global network also offers support for responding to whistleblowing reports in local languages, while complying with the local requirements for handling personal data such as the GDPR (the European Union's General Data Protection Regulations) and PIPL (Personal Information Law of the People's Republic of China). For more information about the Internal Reporting Platform, please click [here](#).

The takeaway

Corporate misconduct is inevitable. Corporations are organisations striving to make a profit in a highly competitive environment. The more loyal employees are to the company, the more they may try to hide any unexpected incident that might occur. Corporate scandals published on the news represent only the tip of the iceberg, and there are many unpublished cases as well, the aftermath of which organisations must deal with. While compliance management to prevent misconduct is important, it is not enough. It is management's responsibility to prepare for possible misconduct and to maintain and operate an effective internal reporting system.

Contact us

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