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By Ben Rowse

Japan's Attempts to Help Banks Vet *Yakuza* Links Fall Short

When Japan's National Police Agency (NPA) announced last January that it would allow Japanese banks to vet potential customers against its closely held database of organized crime or *yakuza* members, the news was met with cautious optimism. The *yakuza* – officially referred to as *boryokudan* (literally, 'violent groups') by the authorities – have long been an embarrassing footnote in the history of corporate Japan. Enabling banks to run the names of potential customers through the NPA's database was initially seen as an important step in cleaning up the corporate landscape.

Membership in a *yakuza* gang is not prohibited. The *yakuza* are legally required to – and do – register their members with police, a reflection of the state's fears of the impact that 'non-organized' crime could have on a society built on order, stability and process. It is illegal, however, for companies, individuals or organizations to engage – knowingly or otherwise – with individuals or entities affiliated with the *yakuza*. While the financial penalties for doing so are negligible, the reputational repercussions can be fatal. Japan's corporate graveyard includes a handful of banks that failed to survive the fallout.

While it represents a step in the right direction, the new disclosure policy is proving insufficient in rectifying the challenge of identifying unsavory customers for multiple reasons. Not least is that only members of the Japanese Bankers Association can avail themselves of the service. Foreign investors and non-Japanese financial institutions cannot search the database, which is accessed via the government-affiliated Deposit Insurance Corporation of Japan. Moreover, searches can only be conducted on customers applying for new account openings. This means that banks are unable to check customers wanting to take out loans and mortgages or those who otherwise raise 'red flags' during the initial intake process. Further constraining the disclosure system is that the list only includes full members of the *yakuza* – of which there were 16,800 as of the end of 2017 – not the 17,700 loosely affiliated syndicate members. The chances of a card-carrying *yakuza* member applying to open a bank account in his own name are somewhere between slim and zero.

Unlike many of its Asian neighbors, where high levels of public sector corruption can represent significant legal risk to investors, exposure to graft is minimal in Japan. Consequently, foreign investors seeking opportunities in the world's third-largest economy often undertake less integrity-focused scrutiny of their potential business partners than elsewhere. Clean bills of health are often assumed simply because it is Japan, and what due diligence is conducted, if any, is often cursory compared to the attention that a similar deal may be subjected to in China or other parts of the region.

This is somewhat understandable when viewed through the anti-corruption lens, but it fails to take into consideration one of the primary risks that investors and local companies alike face when doing business in Japan: unwitting interaction with the *yakuza* or other actors operating on the fringes of organized crime. Few investors will ever find themselves negotiating terms with a tattooed *oyabun* (or *yakuza* godfather). More likely, such negotiations will be with seemingly respectable bankers, lawyers, corporate financiers or other professional advisors, who may be as much in the dark about who they are really working for as is the potential investor. This could be due to a variety of factors including failures in their own client-vetting procedures, Japan's strict data privacy laws that limit disclosure of non-public company shareholders, or willful blindness in the pursuit of profit.

The challenge in Japan is that even those companies that seem to be well established and respectable may in fact be otherwise. Japanese organized crime groups are sometimes collectively described as the country' biggest private equity firm, and operate thousands of front companies. These are not only used for laundering money from their traditional extortion, protection and prostitution rackets, but are also ways to bolster incomes through 'legitimate' businesses.

Understanding the historical interconnectedness of the underworld, the government and corporate Japan is key to appreciating the scale of the problem. For centuries, the *yakuza* have played a role in Japanese society, but in the aftermath of World War II, when they controlled the black market, the syndicates found themselves becoming an important tool in the US's Cold War arsenal in Japan. Because of their position as political allies against the Communist threat and their role in settling personal and commercial disputes outside of the country's elitist legal system, *yakuza* activities were broadly tolerated, both by the authorities and the public respectively. During Japan's economic bubble period of the late 1980s when property speculation soared, the symbiotic relationship that existed between the *yakuza* and some of Japan's largest banks and corporations reached its apogee, and the lines between the legal and illegal blurred. The bursting of the bubble in the early 1990s and growing public resentment at the emboldened nature of the *yakuza's* move into the mainstream economy triggered a gradual crackdown.

Fast forward to today, and despite a tightening of the legislative screws, declining membership, and growing challenges from overseas crime groups looking to muscle in on their turf, the *yakuza* remain deeply entrenched in the fabric of Japan's corporate landscape. Unlike in their heyday, however, *yakuza* bosses are rarely seen publicly hobnobbing with captains of industry, entertainers, sports stars and politicians; instead, they mostly shun the limelight and hide themselves behind shell companies and professional advisers as they seek to diversify their income streams.

The emergence over the past few decades of a new wave of gangsters – often referred to as *hangure* (literally, 'semi-delinquents') – not belonging to the traditional, intensely hierarchical police-registered *yakuza* syndicates further complicates the know-your-customer process. Whilst these quasi-*yakuza* gangs are not covered by existing anti-*boryokudan* legislation and ordinances, their members rarely make the best of business partners from a reputational or trustworthiness perspective.

There is, alas, no easy solution to ensuring that your potential customer or business partner does not have ties to the *yakuza* or other so-called "antisocial forces" beyond old-fashioned sleuthing that marries information in the public domain with human intelligence. Peeling back the layers of corporate obfuscation and connecting the dots where they need to be connected is difficult, time consuming, and usually requires external investigative expertise. But the risks of not conducting proper due diligence in a country where reputation counts for everything, vastly outweigh the costs of doing so.

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