

Overview of the 2024 Amendments to the Japanese Construction Business Act and Their Impact on Contract Price Adjustment

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1. Introduction

On June 7, 2024, the “Bill to partially amend the Construction Business Act and the Act for Promoting Proper Tendering and Contracting for Public Works (Cabinet Bill No. 51)” (the “**Bill**”) was passed by the National Diet (the national legislature of Japan).

This revision aims to secure a stable workforce in the construction industry by introducing measures to:

- (i) Secure wage resources for the improvement of worker treatment in the construction industry and their dissemination to subcontractors,
- (ii) Prevent the burden on contractors regarding labor costs by facilitating the smooth passing on of material price increases to contract prices, and
- (iii) Promote work style reforms and productivity improvements.

The amendments include several provisions that directly affect the contractual relationships between owners¹ and contractors, likely having a significant impact on practical operations.

2. Overview of the Amendments and When They Come Into Force

(1) Overview of the Amendments

- (i) To secure wage resources for improving worker treatment in the construction industry and disseminating these resources to subcontractors, the amendments provide for the following:
 - Contractors are now obligated to make efforts to ensure the proper treatment of workers.
 - The Central Council for Construction Business is tasked with providing and recommending “labor cost standards”.
 - Estimates and requests for estimates based on significantly low labor costs are prohibited.
 - Contractors are prohibited from entering into construction contracts that fall below cost unless there are

¹ Unless otherwise stated, the term “owner” as used in this newsletter includes contractors who subcontract their works to subcontractors.

justifiable reasons, the details of which are to be elaborated by the relevant regulation.

(ii) To prevent the rise in material costs from being absorbed as a cut in labor costs, the amendments provide for the following:

- “Calculation methods for contract price adjustment” in response to material price changes must be specified in the construction contract.
- Contractors must notify owners of information on risks affecting contract prices, such as material price hikes, before entering into the contract.
- If such risks materialize after the contract is signed, contractors may request contract price adjustments according to the stipulated calculation methods, and owners are obligated to make efforts to engage in these discussions in good faith.

(iii) Lastly, concerning work style reforms and productivity improvements, the amendments include the following:

- Contractors are prohibited from entering into contracts with significantly short completion times.
- Requirements for a full-time chief engineer and supervising engineer on-site have been relaxed when information and communication technology (ICT) support is used.
- The government will issue guidelines for site management.

(2) Amendments Affecting the Contractual Relationship Between Owners and Contractors

This section specifically highlights amendments that are likely to impact the contractual relationship between owners and contractors.

The Japanese Construction Business Act as amended by the bill above will be referred to as the “**Amended CBA**”, and the current Japanese Construction Business Act before the amendments will be referred to as the “**Pre-Amendment CBA**”.

(i) Amendments Impacting Worker Treatment Improvement in Contracts

(a) Prohibition of Estimates and Requests for Estimates Based on Significantly Low Labor Costs (Amended CBA, Article 20, Paragraphs 1, 2, 4, and 6)

In addition to the existing effort obligation for contractors to prepare estimates (Pre-Amendment CBA, Article 20, Paragraph 1), the following obligations for both contractors and owners have been added/expanded:

- Contractors' Effort Obligation: When entering into a contract, contractors are obligated to make efforts to prepare a written estimate (“**Estimate with Material Cost, etc.**”), which includes material costs, labor costs and other essential costs to ensure proper work implementation by workers (as prescribed under the order by the Ministry of Land, Infrastructure, Transport and Tourism) (“**Material Cost, etc.**”) and other costs necessary for the construction work (Amended CBA, Article 20, Paragraph 1). These “Material Cost, etc.” described in such Estimate with Material Cost, etc. must not be significantly lower than the normally recognized necessary amount (Amended CBA, Article 20, Paragraph 2).
- Owners' Effort Obligation: Owners are obligated to make efforts to consider the content of the Estimate with Material Cost, etc. when entering into a contract (Amended CBA, Article 20, Paragraph 4) and must not request changes to the Material Cost, etc. that would result in amounts significantly lower than the

normally recognized necessary amount (Amended CBA, Article 20, Paragraph 6).

(b) Prohibition of Below-Cost Contracts for Contractors (Amended CBA, Article 19-3, Paragraph 2)

In addition to the existing prohibition on owners from exploiting their position to enter into below-cost contracts (Pre-Amendment CBA, Article 19-3), the following obligation for contractors has been added:

- Contractors' Obligation: Contractors are prohibited from entering into contracts where the contract price is less than the normally recognized necessary costs for carrying out the construction work, unless there are legitimate reasons such as the contractor's ability to utilize cost-effective materials they possess (which will be prescribed under the regulation of the Ministry of Land, Infrastructure, Transport and Tourism) (Amended CBA, Article 19-3, Paragraph 2).

(c) Prohibition of Contracts with Significantly Short Time for Completion for Contractors (Amended CBA, Article 19-5, Paragraph 2)

In addition to the existing prohibition on owners from entering into contracts with significantly short time for completion (Pre-Amendment CBA, Article 19-5), the following prohibition for contractors has been added:

- Contractors' Prohibition: Contractors are prohibited from entering into contracts where the time for completion is significantly shorter than the normally recognized necessary period for carrying out the construction work (Amended CBA, Article 19-5, Paragraph 2).

(ii) Amendments Regarding the Prevention of Transferring Material Price Increases to Cutting Labor Costs

(d) Obligation to Notify Events Affecting Time for Completion or Contract Price Before Signing (Amended CBA, Article 20-2, Paragraph 2)

In addition to the existing obligation for owners to provide contractors with information on the possibility of events affecting the time for completion or contract price, such as ground subsidence, and information necessary to understand the situation before signing a contract (Pre-Amendment CBA, Article 20-2), the following obligation for contractors has been added:

- Contractors' Obligation: If it is found that there is a risk of significant supply reduction or price increase of material, or other events affecting the time for completion or contract price (which will be prescribed under the regulation of the Ministry of Land, Infrastructure, Transport and Tourism), contractors must notify owners of these risks and provide necessary information for understanding the situation before signing the contract (Amended CBA, Article 20-2, Paragraph 2).

(e) Obligation to Specify Calculation Methods for Contract Price Adjustment in Case of Material Price Increases in Construction Contracts (Amended CBA, Article 19, Paragraph 1, Item 8)

In addition to the existing requirements for construction contracts to include provisions regarding changes in scope of work and contract price due to price fluctuations, the Amended CBA requires specifying the "calculation methods for contract price adjustment" in such cases (Amended CBA, Article 19, Paragraph 1, Item 8).

(f) Effort Obligation to Engage in Good-Faith Discussion on Contract Price Adjustments Based on the Calculation Method (Amended CBA, Article 20-2, Paragraphs 3 and 4)

If the contractor has notified the owner of significant material supply reductions, price increases, or other events affecting the time for completion or contract price as per (d), the following new obligations have been established:

- Contractors' Right to Request Discussions: Contractors may request discussions for changes in the time

for completion, scope of work or contract price based on the specified calculation method (Amended CBA, Article 20-2, Paragraph 3).

- Owners' Effort Obligation: Owners must make an effort to engage in good-faith discussions when such a request is made, unless there are legitimate reasons such as the request being groundless (Amended CBA, Article 20-2, Paragraph 4).

(3) Implementation Timing

The amendments to the Construction Business Act have various implementation timings, which require careful attention. Regarding the amendments discussed in section (2), the implementation timings are as follows:

Provisions effective from the enforcement date, to be specified by separate ordinance within 18 months from the promulgation date:

- (a) Prohibition of Estimates and Requests for Estimates Based on Significantly Low Labor Costs (Amended CBA, Article 20, Paragraphs 1, 2, 4, and 6)
- (b) Prohibition on Below-Cost Contracts for Contractors (Amended CBA, Article 19-3, Paragraph 2)
- (c) Prohibition of Contracts with Significantly Short Time for Completions for Contractors (Amended CBA, Article 19-5, Paragraph 2)

Note: Provision (a) applies only to Estimate with Material Cost, etc. issued after the enforcement date. Provisions (b) and (c) only apply to contracts executed after the enforcement date.

Provisions effective from the enforcement date pursuant to Article 1, item 3 of the supplementary provision to the Bill, to be specified by separate ordinance within 6 months from the promulgation date ("**Item 3 Enforcement Date**"):

- (d) Obligation to Notify Events Affecting the Time for Completion or Contract Price Before Signing (Amended CBA, Article 20-2, Paragraph 2)
- (e) Obligation to Specify the Calculation Method for Contract Price Adjustment in Case of Material Price Increases (Amended CBA, Article 19, Paragraph 1, Item 8)

Note: This provision only applies to contracts concluded on or after the Item 3 Enforcement Date.

- (f) Effort Obligation to Engage in Good-Faith Discussion on Contract Price Adjustments Based on the Calculation Methods (Amended CBA, Article 20-2, Paragraphs 3 and 4)

3. Impact on Practice

As mentioned above, the amendments to the Construction Business Act include provisions prohibiting contractors from entering into construction contracts that fall below cost unless there are justifiable reasons, and obligations regarding the adjustment of contract prices due to price fluctuations. These amendments can impact practice related to claims for increased contract prices due to material and labor cost hikes, which have recently been significant issues in negotiations and causing disputes between owners and contractors.



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