

Control and punishment of employees: a case of Mitsui & Co.

Satoshi Fujimura (Kobe University)

Yasuhiro Shimizu (Kobe University)

I. Introduction

Human resource management is a very diverse activity. Employment and promotion of employees, wage decisions, education and training occupy a very large proportion, but these are not all. Punishment is sometimes required for employees who took unexpected or unfavorable actions or produced unfavorable results. Misconducts of employees and punishment against on them are, necessary but not desired part of the human resource management. In particular, scandals sometimes affect the survival of companies, leave a strong impression on many people, and personnel policy can be effected by scandals.

The prevention of misconducts by employee is a problem of corporate internal control, and it is also a matter of personnel policy. As shown in the fraud triangle theory, companies are obviously required to reduce the opportunities, motivations and justification possibilities for employees to conduct fraud (Dorminey et al., 2012). However, when these risk factors cannot be eliminated completely, the presence or absence of a violation of employees depends largely on the qualities of individual employees. If companies can recognize the risk of violation of employees in advance, it will be of great significance to recruit persons with specific qualifications. We suggest that these qualifications were represented by the academic status.

Historical study on human resource management using longitudinal data tended to focus on personnel systems, salaries or career paths¹. In contrast, this study focuses on the records of punishment in a trading company, Mitsui & Co. in early twentieth century. By focusing on the distribution of the misconducts and scandals, and their relationship with academic career of employees. We show that the rate employees who caused scandals which involved dismissal of employees were those with lower academic degree, and that the management of those days recognized this. Management of Mitsui recognized the merit of hiring graduates in terms of the risk of scandals..

The remainder of this paper is as follows. In the subsequent two sections, we outline the background facts, that is, the characteristics of Japanese education system and personnel system of trading companies in pre-WWII Japan. Section 4 analyzes cases of punishment using the company newsletter as a source and show who and where misconduct causing punishments

¹ Selzer (2001) and Seltzer and Simmons (2001) on Australian banks, and Wakabayashi ed. (2017) on Mitsui & Co.

occurred. In Section 5, we analyze the relationship between misconduct and employee's educational background that causes it, and finally consider the significance of hiring graduates from the perspective of a trading company.

II. Education system in Japan before World War II

Japanese central government, *Bakufu* had restricted the communication and trade with foreign countries from 16th century through mid-19th century. Trades were allowed only with China Korea, and Netherlands, and flow of information and knowledge were limited. Also, since the class system restricted the educational opportunities of people belonging to each social class, the nationwide school system didn't exist for a long time.

Situation changed when the long restricted-door policy was reversed. The new Meiji central government, which succeeded older *Bakufu* after 1868, established a policy to accept the technologies and institutions of the Western countries. Education system was not an exception. In 1872, adopting the French system of education, the government published a basic statement of education system, *Gakusei*, which outlined education system to be adopted nationally, and compulsory schooling was established. After revisions of the basic statements, a basic structure of school was established in early twentieth century.

Education was first divided into three levels, higher education (universities and colleges), secondary education (high school and occupational schools), and primary education (elementary schools). Taken the system in 1919 as an example students are followed the educational pass as following, though the precise name and length of education changed over year. First students of primary school, after six years of compulsory education, had to decide whether they are to proceed to secondary school. Secondary school are also divided into two categories. First one is general course. Students entered middle schools and were to enter institutions of higher education. Second is vocational course. Students entered upper primary school, and some were expected to finish their educations there, or to enter occupational school, such as commercial, industrial, or agricultural schools. Higher education was also divided in universities, higher industrial colleges, and other higher education institutions. Though higher industrial colleges taught same subjects, such as commerce, industry, and agriculture, as secondary vocational schools, entrance by former students of those vocational schools into higher education was severe restricted.

Though school systems were established, the rate of students who received secondary or higher education was low. In 1905, the ratios of students who belongs to secondary schools or higher educational institution in proportion to total population of comparable age were 4.3% and 0.9%, respectively (Ministry of Education, Research Department, 1962, tables 6 and 10). Though the share of students increase over time, even in 1935, they were 39.7% and 3.0%.

Graduates of higher educational institutions were quite small in number.

III. General Trading company (*Sogoshosha*) and their personnel policies

Mitsui & Co. was founded in 1876 and was the largest trading company in Japan in the prewar period. The number of employees was about 1,000 in 1900, about 2,500 in the 1920s and 3,000 in the 1930s (about Mitsubishi Corporation after Mitsui & Co. was about 1,000 in 1920, and other trading companies hired at most several hundreds). The head office of Mitsui & Co. is Tokyo, and in addition to Japan, it has branches and branch offices throughout the world including Europe, North and South America, Asia and Africa, and currently operates as one of the largest general trading companies.

Personnel policy in Mitsui and other trading companies in Japan had common remarkable characteristics irrespective of their scale. First is that employees do not receive different treatment depending on their academic background (Fujimura, 2012, 2014). Japanese companies, especially since the 1960s, were said to treat graduates of higher educational institutions and non-graduates differently. Graduates and others formed distinct groups within the same company both in terms of duties, wages, and other aspects. There is a high wall between graduates and others, and it was extremely difficult to promote across the wall for non-graduates. Even before the war at Kanegafuchi Spinning Company, the largest cotton spinning company in Japan of the day, there are two major groups, university graduates and others, in the distribution of wages, and the influence of educational background was great in deciding wages (Kawamura, Shimizu, and Fujimura, 2015). On the other hand, in trading companies there was no difference in wages and other treatment from the academic background from before the war.

Second is that the proportion of graduates to total employees was extremely high. As seen in the previous section, graduates were quite scarce in Japan before the war. On the other hand, in Mitsui & Co. and other trading companies, the proportion of graduates was prominently high, accounting for a majority of employees.

The question in this paper relates to the second characteristic. Why did the trading company hire a large number of graduates? What are the characteristics of the graduates? If trading companies were expecting characteristics other than the knowledge acquired by education, what is it and why? By focusing on trading companies that hired numerous university graduates we show more clearly the characteristics of graduates with higher education.

IV. Scandals and misconducts in Mitsui & Co.

1. Source

Mitsui & Co. set up rules about punishment of employees in its bylaws. In rule book of 1908, for example, a chapter entitled "punishment" stated that the company shall put penalty, written

reprimand, salary reduction, or dismissal, on the employee who did wrong in violation of the bylaws or orders by his superiors. Clauses regarding punishment remained unchanged in later rule books. Displacements, the severest of the punishment, were applied to serious cases that led to criminal actions and undermined the basis of internal control, and we call these cases “scandals.” Most of the dismissal cases were those regarding illegal financial transaction, including embezzlement, thieving, or bribery.

These clauses were applied to punishment of employee and cases were reported in Company Bulletins (*Shaho*). Bulletins were prepared between 1903 and 1948, except the confusion of several months after Great Kanto Earthquake in 1923. Each bulletin had about four pages, and it reported many internal matters, including hiring and retirement, business trip, promotion, relocation, and punishment of employees, establishments and closures of branch offices. 200 or 300 bulletins were prepared each year, and the share of punishment bulletin was small. An example of punishment is as follows (*Shaho*, No. 109):

Punishment

HK², branch manager of Moji,

did construction outside the budget without applying to the head office in constructing Wakamatsu subbranch office. Reprimanded due to unsuitable action. Be cautious henceforth.

July 1, Meiji 36 [1903]

When a bulletin report a punishment, the person to be punished, the reason for punishment, and the penalty were generally stated in it. Most bulletins stated the reason for punishment in general terms. In considering the punishment cases, there are two approaches to treat scandals and misconducts. One is to treat the two as different nature. Misconducts are rather common events arising from daily business operations and punishments on them are usually written reprimand or salary reduction. Scandals are, in contrast, extreme rare cases and led to compulsory dismissal of employees. However, distinction between misconducts and scandals is not always clear. Scandals are sometimes extensions of misconducts. In this paper we take the latter position and treat scandals as extreme cases of misconducts.

2. Overview of punishment cases

According to Corporate Bulletins, the company punished 132 people in 67 cases between 1903 and 1948, including 19 scandals are where 21 employees were punished. We next analyze these cases in terms of academic background and geography of employees.

² Name of employees are stated in initials.

(1) Academic ground

Table 1 shows the distribution of punishment and academic background of employees punished. Academic background was identified with the last of educational institution an employee graduated from. It is divided into higher education, secondary education, primary education, and unknown, and higher education status was subdivided into Imperial universities, higher commercial colleges, and others.

Of 132 employees who were punished, 90 (70%) are graduates of the higher academic institutions, 19 completed secondary education, and 11 elementary education. Other 10 were employees of lower classes who were hired in local offices or who worked by the day, whose academic status is secondary or primary school graduate³.

Penalties on employees with higher education records were generally not severe. 32 reprimands and 44 salary reductions of one month, and only four employees were dismissed, and only one was dismissed because of embezzlement. Few graduates were involved in scandals. This shows a sharp contrast with the employees with lower educational status. Of 40 employees with secondary or primary education, 21 were punished by reprimands and salary reduction of one month, while 16 were dismissed.

Table 2 shows the relationship between the reason for punishments and academic background of employees punished. We divided the reason into four categories: breach in trading activities, breach in general administration, supervisory responsibility, and embezzlement. It shows that the most frequent reason for punishment was supervisory responsibility and most of the employees punished by supervisory responsibility were those with higher education. Of 58 employees punished by supervisory responsibility, 45 had higher education, most of whom were branch managers or divisional managers. Penalties on them were generally reprimand and salary reduction. Punished by embezzlement were 15, of whom 12 were with secondary or primary education.

We must understand these numbers with the total number of employees to fully understand the significance of education. If the number of employees with secondary or primary education was large, the number of punishment should be proportionally large. However, Mitsui & Co. had a large share of employees with higher education. In 1913, of 1977 total employees, those with higher education were 482 (24.3%), secondary education 156 (7.9%), and primary education 235 (11.9%), local recruitment or daily-wage employees 550 (27.8%) (Fujimura, 2014). In later years, the share of graduates increased dramatically. In 1916, 806 (53.2%) out of 1,514 employees were graduates, and 1,586 (64.0%) out of 2482 in 1926, 1,727 (64.5%) out of 2680.

³ Graduates of higher educational institutions were not hired by local offices, or worked by day.

Most scandals, however, were perpetrated by those with lower education. Of 19 scandals involving 21 employees, only four were those with higher education, and 16 with lower educational status. There are clear relationship between academic status, severances of punishment, and the reason for punishments.

It should be noted that the academic status of employees itself was not considered in each case. It is shown in two scandals which happened in 1919 and 1938 in New York branch office. Both were cases where huge losses happened due to unauthorized future contracts and employees in charge were dismissed. In 1919 case the dismissed employee graduated secondary school (Kobe commercial school) and in 1938 case it was a graduate of a higher educational institution. The company had a personnel policy to treat employees equally without regard to their academic status in terms of wages and career paths. Punishments were imposed in a similar fashion. If the company had treated employees with different academic status differently due to the academic status, it would have led to corruptions of graduate employees. Equal treatment of employees was necessary as a control mechanism.

(2) Geographic distribution

In this section, to grasp the geographical distribution of cases of punishment, the place of occurrence of violation cases is analyzed chronologically. Table 3 shows the occurrence areas of violation cases by age. Breaching often results in punishment not only for the employee at the location where the violation occurred but also for the supervisory responsibilities of the employees of the Tokyo head office. Therefore, in Table 3, only the employees of the violation at the time when the violating act originally occurred are counted (in one case an employee was punished due to two causes and we count them separately). Also, in order to clarify the geographical distribution of scandals, the number of scandals was noted in brackets.

The place of occurrence of violation was classified in the head office, branch offices in Japan, China / Korea, Asia other than China / Korea (Southeast Asia and India etc.), Europe, North America. The head office is located in Tokyo, and various domestic branches are branch offices and branch offices in Yokohama, Osaka, Nagoya, Kobe and so on. In addition to large branches such as Shanghai and Hong Kong, many small subbranch offices were set up in the China / Korea region. Business in European region was centered on the London branch, and there were (sub)branch offices in several cities. The North American base is located in New York, San Francisco, Seattle and others.

The violation tended to occur abroad. Prior to the end of the World War I (1903 - 1919) many violations occurred in Japan, but the number of offenders in Japan since that time has decreased dramatically. On the other hand, since World War I, the absolute number of offenses decreases abroad, but the number of violations remained to be more than those in Japan. The

disparity of the occurrence of violation is more pronounced when compared with the geographical distribution of employees. In Mitsui & Co., throughout this era, employees in Japan accounted for 60 to 70% of the total, while overseas employees were 30 to 40%. In addition, 20% of the employees belonged to the Tokyo head office, but violations have hardly occurred there. Less employees generated more violations abroad. The place of scandals were neither uniform. Where the 5 employees were punished by scandals which happened in Japan, 16 were punished by those happened overseas. The distance from the center of the organization accelerated the difficulty of control.

When examining the area in more detail, it is clear that many violations occurred in China / Korea. More than 40% of penalized employees and more than half dismissed caused violation there. Furthermore, the single case where the branch manager was dismissed occurred in the same area. The branch manager who was punished in this case caused a huge loss due to neglected accounts receivable against the authorities of the Qing Dynasty and improper exchange processing. He sent a false report to the head office, and was fired by maliciousness of false report. The reason why the violation acts concentrated in China and the Korea region is not yet clear, but the violation may also be affected by the degree of clarity of the counterparty.

In time series, the number of misconducts decreased. In terms of the number of punished employees per year, the average annual rate declined 2.9 people before 1919 to 0.7 since 1920. Since the total number of employees increased from 732 in 1905 to 2935 in 1935, the number of violations per employee dropped sharply. When considering violation cases individually, it is found that the number of violations themselves has decreased since the company has not lowered criteria of sanction. The decline in the number of violations would be the result of multiple reasons, but it is possible the greatest factor was strengthening of internal discipline. The fact that the company in the Meiji era was extremely cluttered was pointed out at the *Minutes of Branch Managers' Meeting (Shitencho Kaigi-roku)* in 1906. Prior to World War I, clothes and working hours of employees were not controlled and were uneven. As internal organizations were improved, clarification and documentation of division of duties and standardization of risk management procedures were carried out. Employees began to work according to rules and norms of the company, which may have resulted in a violation. However, the rate of decrease in scandals involving dismissal was small compared to that of general violation. It seems that it was difficult to completely prevent scandals at overseas branches.

V. Analysis

As we saw in the previous section, there was a clear relationship between scandals and employees' academic background. Briefly, most of the scandals have occurred by employees with only secondary or primary education, and it was rare for employees of graduates to cause

scandals. It should be noted that the fact that management at that time knew the characteristics of such distribution of scandals. The following materials are part of the *Minutes of Branch Managers' Meeting* held at the Tokyo headquarters in 1913.

From now on I think that the company shall hire highly educated people to our employees. One of the drawbacks of personnel system of the company is to promote chore boys to regular employee and I want to abolish this system. As far as I know, the performances of those who raised from chore boys and those who are not well educated are generally low. And, in reality, often abusive scandals inside the company are often caused by those. Those who have not received good education do not have little character, so it is impossible to trust and leave their jobs to them (quoted from Wakabayashi, 2007, 48).

This is a part of the remark made by the personnel manager, Yoshiro Fujimura⁴. He linked the academic status of employees and the scandals, and stated his desire to increase the hire of graduates of higher education.

Behind his remarks there were big scandals. In the previous year, two serious scandals occurred consecutively. One is called "Yokohama shipping handling office case," where a teller forged internal documents, issued and obtained checks by deception, and embezzled 90,000 yen⁵. The other was called the "Nagoya incident," and brought further serious effects to the company. The employee in charge of accounting at Nagoya branch office conspired with the external stock broker to forge the promissory note of the branch and exploited 800,000 yen from four banks in Nagoya area. Many newspapers covered the incident every day after its revelation. Depositors rushed to banks and withdrew their deposits, which triggered a run on the banks. The confusion was so great that the police officers went out, and the Bank of Japan decided to make emergency lending. The company was suffered by a tough criticism, and it had not only to compensate for the counterfeit bills against banks, but also to do import and export without bills of exchange, probably because the bank seemed to have boycotted the handling of the bills as sanctions. There was a serious trouble in the trading business. Those two scandals were perpetrated by employees with secondary or primary education. The remarks by Fujimura were based on the occurrence of such scandals. Consequently, personnel policy was promoted based on the recognition that the subjects of the scandal were employees with the middle or primary education.

⁴ His position in Japanese is *Kacho*, which is ranked next to top management, although it now means a middle management. Fujimura himself was from an aristocratic family and a graduate of Cambridge university, and was promoted to the position of the director in 1918.

⁵ The amount is about 1 million dollars in present value.

In general, trading companies were vulnerable to violation by individual employees. It is essential to establish branch and subbranch offices abroad, and a large discretion is given to employees who work there. Employees were able to execute huge transactions at their own discretion. Control from the headquarter office was not easy due to the distance between offices, and the efforts of the headquarter office to control branch and subbranch offices were in some cases nullified deliberately. A famous scandal that was caused by the lack of management was the bankruptcy case of Furukawa Shoji, the biggest trading company after Mitsui (Takeda, 1980). The director of the Dalian subbranch office had continued futures trading of soybean cake without authorization for a long time. The resulting loss from those trades reached several times of the capital stock of the company, resulting in the sudden bankruptcy in 1920. The Tokyo headquarters had conducted audits of the Dalian subbranch multiple times but was unable to find illegal transactions, because of the falsification of account books and forgery of transaction records by the manager of the subbranch office.

In Mitsui, disciplinary consciousness of the graduate employees was evaluated as one of the important utilities of higher education. This had been formed through experience of scandals. In order to prevent scandals, it is necessary to construct a group of employees with high ethics, and recruitment of graduates of higher education is thought to promote the formation of disciplinary consciousness. Fujimura's remarks clearly recognize that recruitment of graduates brought discipline within the company, and as a result, in Mitsui, and many other trading companies, the structure of employees that graduates occupies a majority.

VI. Conclusion

In this paper, we focused on misconducts and scandals at Mitsui. Mitsui had a long-established policy to treat employees impartially regardless of their academic status, and the policy was also applied to punishment. In total number of punishments, graduates accounted for about two thirds of employee punished, punishments on them were relatively light. In contrast, scandals that lead to dismissal of workers centered on employees with lower academic status. Although number of misconducts in Mitsui decreased with the passage of time, the relationship between the academic status of employees and scandal remained and the recollection of scandals led its management to hire more graduates.

Many studies that examined the reason why a company employs those with higher education pointed out expert knowledge such as language and human network of academic window. Becker-type arguments about utilities of higher education also centered on these topics (Becker, 1993). In this paper, however, it is suggested that the high sense of discipline was also an important factor. Of course, not all of higher education is aimed at cultivating discipline consciousness. Some studies pointed out that business schools does not train ethics and

graduates have low ethical standards. However, the degree is acquired at the end of a long disciplined education, and opportunistic behavior is never effective in it⁶. Sense of discipline was cultivated in their mind and the company could be aware of it.

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⁶ Large number of employees hired by Mitsui graduated from commercial college. Macfarlane (1995) argues that

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Table 1 Penalties by educational background

Unit: Number of people

Academic background/Origin	General misconducts			Scandals	Request for retirement	Total
	Reprimand	Salary reduction		Dismissal		
		1 month	3 month			
Higher education						
Imperial University	7	5	0	0	1	13
Higher Commercial college	22	34	7	0	1	66
Others	3	5	1	0	0	11
Subtotal	32	44	8	0	2	90
Secondary education						
Secondary education	4	7	2	0	0	19
Primary Education	4	2	0	1	0	11
Local recruitment / daily-wage	2	2	0	0	0	10
Subtotal	10	11	2	1	0	40
Unknown						
Unknown	0	0	1	0	0	2
Total	42	55	11	1	2	132

Sources: Mitsui & Co., *Shaho*, 1903-1948.

Table 2 Penalties by reason and academic background

Unit: Number of people

Academic background/Origin	Breach in trading activities	Breach in general administration	Supervisory responsibility	Embezzlement	Total
Higher education					
Imperial University	2	3	8	0	13
Higher Commercial college	27	12	31	0	70
Others	3	0	6	2	2
Subtotal	32	15	45	2	94
Secondary education					
Secondary education	5	2	9	4	20
Primary Education	2	4	2	4	12
Local recruitment / daily-wage	1	4	2	4	11
Subtotal	8	10	13	12	43
Unknown					
Unknown	1	0	0	1	2
Total	41	25	58	15	139

Sources: Mitsui & Co., *Shaho*, 1903-1948.

* In seven cases, multiple reasons for punishment were recorded, and each separate reason was counted.

Table3 Penalties by region

Unit: Number of people

Period	Head office	Domestic	Asia (except		Europe	North America	Total
			China / Korea	China/ Korea)			
1903-1904		5[1]	3	1			9[1]
1905-1909		5[1]	11[3]		1		17[4]
1910-1914	3	3[2]	6[4]			1	13[6]
1915-1919		1	7[3]			2[1]	10[4]
1920-1924			1	2	2[2]	1	6[2]
1925-1929			1	2			4[0]
1930-1934			1				1[0]
1935-1939		1[1]	1[1]	2		1[1]	5[3]
1940-1948		1	1	2[1]			4[1]
Total	3	16[5]	32[11]	10[1]	3[2]	5[2]	69[21]

* Numbers in brackets are the numbers of dismissed employees because of scandals. In one case, multiple reasons for punishment were recorded, and each separate reason is counted.