Japan

Masakazu Iwakura and Tomohiro Takagi
Nishimura & Asahi

www.practicallaw.com/7-501-9661

MARKET AND REGULATION

1. Please give a brief overview of the public M&A market in your jurisdiction. (Has it been active? What were the big deals over the past year? Please distinguish between trade buyers and private equity backed deals.)

In 2009, the number of M&A transactions in which Japanese companies were involved was reportedly about 2,800, the total value of which was reportedly about US$128 billion (about EUR93.86 billion). Because of the worldwide financial crisis, the number of M&A transactions in Japan fell by about 5% in 2009 as compared with 2008. In particular, the number of transactions invested in by offshore entities fell by about 10% in 2009 as compared with 2008, and the value of transactions invested in by offshore entities fell to about 20% in 2009 as compared with 2007 when the value of transactions invested in by offshore entities was the highest ever.

The big deals announced or completed over the past year include the following:

- In October 2009, Sumitomo Mitsui Banking Corporation acquired all of the shares of Nikko Cordial De-merger Preparatory Company Ltd. (new Nikko Cordial Securities Inc.), which had succeeded to all of the operations of the former Nikko Cordial Securities Inc. and certain businesses of the former Nikko Citigroup Ltd. through a corporate de-merger from Nikko Citi Holdings, Inc., a wholly owned subsidiary of Citigroup Inc. The transaction value was reportedly about US$6.4 billion (about EUR4.7 billion).
- Mitsubishi UFJ Financial Group, Inc. (MUFG) and Morgan Stanley (MS) jointly announced:
  - in March 2009, that they had signed a memorandum of understanding (MOU) to form a securities joint venture combining Mitsubishi UFJ Securities Co., Ltd. (MUS) and Morgan Stanley Japan Securities Co., Ltd. (MSJS). MUFG will hold 60% and MS will hold 40% of the joint venture;
  - in November 2009, that they are pursuing a joint venture structure involving two entities:
    - Mitsubishi UFJ Morgan Stanley Securities Co., Ltd., which will be 60% owned by MUFG and 40% owned by MS, is expected to include the wholesale and retail businesses of MUS and the investment banking operations of MSJS; and
    - Morgan Stanley MUFG Securities Co., Ltd., of which a 51% voting interest will be owned by MS and a 49% voting interest by MUFG (while the respective economic interests of MUFG and MS in such company are expected to be 60% and 40%), is expected to include the existing operations of MSJS (excluding the investment banking operations).
  - in March 2010, that they had entered into definitive agreements to integrate their securities operations in Japan, and are expected to commence joint venture operations as of 1 May 2010.
- In December 2009, Panasonic Corporation completed the public takeover of Sanyo Electric Co, Ltd in the electric industry. The transaction value was reportedly about US$4.5 billion (about EUR3.3 billion).

2. What are the main means of obtaining control of a public company? (For example, public offer, legal merger, scheme of arrangement and so on.)

Stock purchase

Shares of a listed target company (target) can be purchased through the stock exchange or outside the stock exchange. This must be done by a public offer in some situations (*see Question 4*). This method does not require an agreement with the target's board, and therefore can be used for hostile bids. Foreign companies can also use this method.

In addition, a proxy fight (where a group of shareholders is persuaded to join forces and gather enough shareholder proxies to win control of a company) can be used as a method of takeover.

Merger and stock-for-stock exchange

These methods of obtaining control require an agreement with the target's board, and therefore are only used for recommended bids.

Merger. A merger integrates two or more companies into one corporate entity (*Article 748, Corporate Law*).

The shareholders of the absorbed company are usually allotted shares in the absorbing company according to the merger ratio (which is based on multiple factors, including the corporate value of the absorbed company relative to that of the absorbing company).

Foreign companies cannot use this method to obtain control of a company.

Country Q&A

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

Stock-for-stock exchange. This is where Company A becomes an absolute parent company of another company (Company B), by issuing new shares in itself in exchange for all of the shares in Company B (*Article 767, Corporate Law*).

Foreign companies cannot use this method to obtain control of a company.

However, by using a triangular merger (in which a subsidiary absorbs and merges with the target, and provides shares of its parent company to shareholders of the absorbed target), a subsidiary of a foreign company in Japan is able to absorb a Japanese company by using its parent company's shares (*Articles 749.1(2) and 751.1(3), Corporate Law*). In addition, a stock-for-stock exchange, in which the parent company's shares are used for consideration, is allowed (*Articles 768.1(2) and 770.1(3), Corporate Law*).

Issue of new stock and business transfer

Issue of new stock. The acquiring company makes a subscription agreement with the target and receives new shares issued by the target (*Article 199, Corporate Law*).

There are potential problems, namely that minority shareholders remain and more funds are needed to obtain control of the target in an issue of new stock than in a stock purchase. The issue of new stock is available to foreign companies.

The issue of new stock requires a decision by the target's board, and therefore cannot be used in a hostile bid. In addition, in the case where a listed company issues new shares at a ratio of 25% or more of the issued shares, the company must obtain either (*Article 432, Security Listing Regulations*):

- An opinion from an independent person from the company's management regarding the necessity and reasonableness of the issuance.
- The shareholders confirmation of the decision to issue new shares (for example, from a shareholders' meeting).

Business transfer. An acquiring company takes over part or parts of a business, composed of the target's integrated assets, employees, commercial rights and so on (*Article 467, Corporate Law*). A business transfer is used when a company intends to selectively pick which assets and debts to acquire.

3. Are hostile bids allowed? If so, are they common? If they are not common, why not?

Hostile bids are allowed. They can be made by a stock purchase. The number of hostile bid attempts is increasing, although almost all are unsuccessful.

Until 2000, hostile bids were not common, partly because of the deep-rooted cross-shareholding among Japanese companies and the resistance to hostile bids within Japanese society. However, after 2000, the number of hostile bids started to increase, mainly due to the dissolution of cross-shareholding among companies, and a change in attitudes towards hostile bids or takeovers by foreign companies.

Recent examples of hostile bids are:

- The Steel Partners Japan Strategic Fund's bid for Bull-Dog Sauce in 2007, which failed due to defensive measures taken by the target (with shareholders' approval).
- The Ken Enterprise's bid for Solid Group Holdings, also in 2007. The Ken Enterprise's hostile bid was the first case in Japan in which a hostile tender-offer bid succeeded despite the opposition of the target's board.

4. How are public takeovers and mergers regulated and by whom?

Regulation of public takeovers

Public takeovers are regulated by the Financial Instruments and Exchange Law (FIEL). If a party intends to purchase shares of companies that are required to submit annual security reports (including listed companies and over-the-counter (OTC) companies), this must be done by public offer in the following cases (with several exceptions):

- If the purchase is made outside the stock exchange market (including the OTC security market) and, after the purchase, the aggregate voting rights held by a buyer and any affiliated persons (as defined in the FIEL) divided by the total voting rights of the target (total voting ratio) exceeds 5% (*Article 27-2.1 (1), FIEL*). An exception applies if the aggregate number of sellers in the contemplated share purchase and the sellers of shares to the buyer outside the stock exchange market (total sellers) equals ten or less in the 60 days before the day the purchase is made.
- If the purchase is made outside the stock exchange market (including the OTC market), the number of total sellers is ten or less and the total voting ratio exceeds one-third after the purchase (*Article 27-2.1 (2), FIEL*).
- If the total voting ratio exceeds one-third after the purchase, and the purchase is made by the methods of purchase prescribed by the Prime Minister (including purchasing through Tokyo Stock Exchange Trading NeTwork System (ToSTNeT) of the Tokyo Stock Exchange and certain off-floor trading methods) (*Article 27-2.1 (3), FIEL*).
- If, within three months:
  - over 5% of the voting shares are purchased outside the stock exchange market (including the OTC security market) or by the methods of purchase prescribed by the Prime Minister mentioned above;
  - a total of over 10% of the voting shares are obtained through purchase (including purchases described in the preceding bullet point) or the issuance of new shares; and
  - the total voting ratio exceeds one-third after the purchase or the issuance (*Article 27-2.1 (4), FIEL*).
- If, during the period in which another party's public offer is made, a party, whose total voting ratio before the purchase exceeds one-third, purchases over 5% of the voting shares (*Article 27-2.1 (5), FIEL*).

Country Q&A

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

- In other specified cases set out in a cabinet order (*Article 27-2.1 (6), FIEL*).

There is no institution in Japan that corresponds to the Takeover Panel in the UK. The Financial Services Agency (FSA) supervises the securities markets (*see box, The regulatory authority*).

Regulation of mergers

Mergers are regulated by the Corporate Law. The following are required for a merger:

- Conclusion of a merger agreement (*Article 748, Corporate Law*).
- Advance disclosure of certain documents, including the merger agreement (*Articles 782 and 794, Corporate Law*).
- Approval of the shareholders' meetings of the merging companies (*Articles 783 and 795, Corporate Law*).
- Procedures to protect creditors (*Articles 789 and 799, Corporate Law*).
- Procedures to resolve share purchase demands from dissenting shareholders (*Articles 785 and 797, Corporate Law*).
- Registration of a merger (*Articles 921 and 922, Corporate Law*).
- Disclosure of certain matters after the merger (*Articles 791 and 801, Corporate Law*).

Where shares are issued or delivered through a corporate reorganisation (including merger) that satisfies certain conditions, the issuer of the shares must make disclosure on issuance or delivery of the shares (by submitting a security registration statement) (*Article 4.1, FIEL*). After that, it must make the continuous disclosure prescribed in the FIEL if the disclosure is (*Article 24.1(3), FIEL*):

- Made concerning shares of the target of the reorganisation.
- Not made concerning shares that will be issued or delivered to shareholders of the target through the reorganisation.

PRE-BID

5. What due diligence enquiries does a bidder generally make before making a recommended bid and a hostile bid? What information is in the public domain?

Recommended bid

A bidder undertakes business, accounting and legal due diligence. It receives various information and documents as agreed between the bidder and the target (for example, important contracts, board minutes, licences and approvals, and documents about contingent liabilities), and information and documents in the public domain.

Hostile bid

In general, a bidder's due diligence is based on information in the public domain.

Public domain

There are several different sources of public information.

The Commercial Register. This contains the following information on all companies (*Article 911.3, Corporate Law*):

- The company's purpose.
- The trade name.
- The amount of stated capital.
- The total number of issued shares, and the classes and the number of them.
- The contents and number of each class of shares. If a transfer of shares requires the approval of the company, the Commercial Register also includes the provisions for the transfer from the articles of incorporation.
- The organisation of bodies of the company.
- The names of the directors.
- The way the company provides public notices and other information.

Accounts. The following are publicly available:

- The target's balance sheet. Balance sheets of a joint stock company (*kabushiki kaisha*) are made public through a public notice or its website (*Article 440, Corporate Law*).
- Income statements for a large company (a company with a capital of JPY500 million (about US$5.6 million) or more, or liabilities of JPY20 billion (about US$225 million) or more) (*Article 440, Corporate Law*).

Annual and quarterly (or semi-annual) securities reports. Listed companies, OTC companies and certain other companies must file annual securities reports and quarterly securities reports (or semi-annual reports). Annual securities reports contain the following information (*Article 24, FIEL*):

- An outline of the company, including changes in major business indices, the history of the company, structure of the business, status of the related companies and status of employees.
- The condition of the business, including an outline of business results, production, orders and sales, problems to be resolved, risk factors and material contracts.
- The condition of the company's facilities, including an outline of business investment, the condition of principal facilities and plans for installation or removal.
- A description of the company, such as information about shares (including the total number of shares, changes in the number of issued shares and the capital, type of shareholders and major shareholders), dividend policy, directors and officers, and corporate governance.
- Accounting conditions.

It is also possible to obtain, from annual securities reports, information about a rights plan as a defence measure against hostile bids.

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

Quarterly securities reports (or semi-annual reports) contain similar information to that contained in the annual securities reports (*Articles 24-4-7.1 and 24-5.1, FIEL*).

In addition, the articles are attached to the annual securities report, and can be inspected by anyone.

Extraordinary reports. A company that must file an annual securities report must also file with the Prime Minister, without delay, an extraordinary report if it intends to make a public offering or secondary offering in a foreign country, or if required under Cabinet Office regulations (*Article 24-5.4, FIEL*). Cabinet Office regulations require such a report in the case of:

- A change of the company's main shareholder.
- A disaster affecting the company.
- A determination on a stock-for-stock exchange, stock transfer, corporate demerger, merger, business transfer and so on.

The extraordinary report serves as the means of publicising those events (*Article 25, FIEL*).

Timely disclosure. Disclosure regulations of the stock exchange or a securities dealers' association require that listed companies and OTC companies make timely disclosure of information to investors that may impact on their investment decisions. Information that must be disclosed includes (*Tokyo Stock Exchange, Security Listing Regulations*):

- Certain items determined by the company or its subsidiaries. This includes a reduction of capital, a stock-for-stock exchange, a stock transfer, a corporate demerger or merger, and a business transfer and dissolution.
- Certain facts affecting the company or its subsidiaries. This includes damages caused by a disaster or damages that have occurred in business operations, a change of the main shareholder and any event that may cause de-listing.
- Account settlement by the company or its subsidiaries.

6. Are there any rules on maintaining secrecy until the bid is made?

There are no rules on maintaining secrecy until the bid is made. However, in recommended bids, the parties often conclude confidential agreements, obliging them to keep matters confidential.

7. Is it common to obtain a memorandum of understanding or undertaking from key shareholders to sell their shares? If so, are there any disclosure requirements or other restrictions on the nature or terms of the agreement?

Bidders often obtain a memorandum of understanding or undertaking from key shareholders to sell their shares (or to apply for a public offer).

A listed company must disclose certain matters when an "organ of administrative decision", including a board, decides to make a public offer, or makes another important decision about, for example, its management, operation or assets (*Stock Exchange Rules*). Accordingly, a party may be required to disclose that it has entered into a memorandum of understanding and/or certain elements of the agreement (*see Question 12*).

In addition, under certain conditions, the bidder must disclose an agreement with key shareholders as an important agreement concluded regarding the shares in the registration statement of a public offer (*see Question 12*).

8. If the bidder decides to build a stake in the target (either through a direct shareholding or by using derivatives), before announcing the bid, what disclosure requirements, restrictions or timetables apply? Are there circumstances in which shareholdings, or derivative holdings, of associates could be aggregated for these purposes?

Disclosure requirements

A holder of securities (issued by a listed company, including an OTC company) whose shareholding is larger than 5% (including a holder of options to obtain a shareholding larger than 5%) (Large Shareholder) must:

- File a large shareholding report within five days of the day on which it became a Large Shareholder (*Article 27-23, FIEL*).
- Send, without delay, a copy of the report to the company that issued the shares and the stock exchange or securities dealers association (*Article 27-27, FIEL*).
- File an amendment report if its shareholding has increased or decreased by 1% or more after becoming a Large Shareholder (*Article 27-25, FIEL*).

The number of shares held by the bidder and joint shareholders are aggregated to calculate this shareholding for filing a large shareholding report and an amendment report (*Article 27-23.4 to 6, FIEL*). An entity is a joint shareholder if it either:

- Has agreed with the bidder that purchases the shares to jointly acquire or transfer those shares, or to jointly exercise voting rights or other rights.
- Is in a relationship of share ownership, kinship or other special relationship with the bidder that purchases the shares, as set out in a cabinet order.

Regulations

Shareholders with 3% or more of the voting rights or issued shares can demand to inspect or copy the accounting books and materials (*Article 433, Corporate Law*). These shareholders fall into the category of a corporate insider.

If a corporate insider becomes aware of a material fact about the listed company when exercising its inspection rights, the corporate insider cannot purchase, sell, assign or acquire for value any security of the listed company, until the material fact has been made public (*Article 166.1(2), FIEL*).

In addition, if a shareholder is a main shareholder (holding 10% or more of the voting rights) of a listed company, the following apply:

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

- If a main shareholder purchases or sells securities of certain issuers, it must file with the Prime Minister a report of this, no later than the fifteenth day of the month after the purchase or sale (*Article 163.1, FIEL*).
- A listed company can demand a main shareholder to surrender to it any profit that the main shareholder has made for its own account by selling, within six months of purchase, a security of the listed company (or by purchasing such a security within six months of sale) (*Article 164.1, FIEL*).
- A main shareholder of a listed company cannot execute a short sale of shares exceeding the amount of shares it owns (*Article 165, FIEL*).

9. If the board of the target company recommends a bid, is it common to have a formal agreement between the bidder and target? If so, what are the main issues that are likely to be covered in the agreement? To what extent can a target board agree not to solicit or recommend other offers?

Traditionally, it was not common to have a formal agreement between the bidder and the target. This may have been because all agreements between the bidder and the target must be disclosed in the registration statement of a public offer (*Article 12 and Form No. 2, Cabinet Office Regulation Concerning Disclosure in a Public Offer by Entities Other Than the Issuer*) (*see Question 12*).

Recently, however, the number of cases in which the bidder and the target have a formal agreement has begun to increase. In those cases, the main issues that are likely to be covered in the agreement include:

- The target's obligation to express its approval of the public offer and not to solicit or recommend other offers.
- The break fee.
- The so-called fiduciary-out provision (*see below*).
- Rules after the public offer has been completed (including rules of selection of the target's board members, the target's dividend policy, and the relationship between the bidder and the target).

The target must, under Cabinet Office regulations, file with the Prime Minister a document stating its position on the public offer and other matters required by Cabinet Office regulations (Position Report) within ten business days of the date of the public notice of the start of a public offer (*Article 27-10. 1, FIEL*) (*see Question 12*).

As a result, the agreement between the bidder and the target can include provisions obliging the target to express its approval of the public offer.

In this regard, directors of a company must perform their duties with the care of a good manager and owe a duty of loyalty to the company (*Articles 330 and 355, Corporate Law* and *Article 644, Civil Law*). The board can agree not to solicit or recommend other offers if this is in compliance with its duties.

Therefore, if the target makes an agreement with the bidder, from the viewpoint of the target's directors it is advisable to establish "fiduciary out" provisions in the agreement that allow the target to obtain a release from that agreement if a third party makes a better offer for the target, as the target's directors would violate their duties if they did not recommend the third party's offer.

10. Is it common on a recommended bid for the target, or the bidder, to agree to pay a break fee if the bid is not successful? If so, please explain the circumstances in which the fee is likely to be payable and any restrictions on the size of the payment.

It is not yet common on a recommended bid for the target or the bidder to agree to pay a break fee if the bid is not successful. One reason for this is that the target or the bidder cannot control whether or not a bid succeeds.

However, there has been an increase in the number of cases in which the target agrees with the bidder that the target will express its approval of the public offer and will not solicit or recommend other offers (*see Question 9*). The agreement can provide that if the target breaches this requirement, it must pay a break fee. There are no restrictions on the size of the payment in such cases.

11. Is committed funding required before announcing an offer?

Committed funding is required before announcing an offer subject to the following:

- A bidder must disclose information about funding in the registration statement of a public offer (*Article 12 and Form No. 2, Cabinet Office Regulations Concerning Disclosure in a Public Offer by Entities Other Than the Issuer*) (*see Question 12*).
- A bidder must also file a document indicating that it has the necessary funds in relation to the offer (this includes its bank balance). This is attached to the registration statement (*Article 13.1.(7), Cabinet Office Regulations Concerning Disclosure in a Public Offer by Entities Other Than the Issuer*).

However, guarantees by financial institutions are not required, nor is the joint liability of financial advisers.

ANNOUNCING AND MAKING THE OFFER

12. Please explain how (and when) the bid is made public (highlighting any relevant regulatory requirements) and set out brief details of the offer timetable. (Consider both recommended and hostile bids.) Is the timetable altered if there is a competing bid?

Timely disclosure based on stock exchange regulations

If the applicant making a public offer is a listed company, it must disclose the following immediately after the board or other decision-making body decides to make the offer (*Tokyo Stock Exchange*

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

regulations, Article 402(1)x, Security Listing Regulations and *Part 2, Chapter 1, section 11(2) of the Timely Disclosure Guidebook*):

- Purpose of the purchase.
- Description of the target.
- Public offer period.
- Purchase price.
- Grounds for calculating the purchase price.
- Number of shares to be purchased and other information concerning the public offer.

Public notice of the start of a public offer

If an entity must purchase shares by way of a public offer (*see Question 4*), it must serve a public notice containing information on the following (*Article 27-3.1, FIEL* and *Article 9-3, Cabinet Order for Enforcement of FIEL (COEF)*):

- Purpose of the public offer.
- Purchase price.
- Number of shares to be purchased.
- Public offer period.
- Any other matters required by Cabinet Office regulations.

As a general rule, a bidder cannot, after it has served a public notice regarding the start of a public offer, withdraw the offer or cancel the offer contract. However, shareholders who accepted the offer can cancel a contract entered into in connection with that offer at any time during the offer period (*Article 27-11.1 and 27-12.1, FIEL*).

Filing of public offer registration statement

On the same day as an entity serves a public notice (*see above, Public notice of the start of a public offer*), Cabinet Office regulations require that it file with the Prime Minister a registration statement of a public offer, setting out:

- The offer conditions (including the grounds for calculating the purchase price).
- The contents of any agreement in which the bidder, after issuing a public notice regarding the start of a public offer, agrees to purchase the target's shares by a method other than the public offer.
- The purpose of the offer. (If there is a prospect of de-listing, it must also disclose this prospect and its reasons.)
- Matters concerning the bidder.
- Any other matters required by Cabinet Office regulations.

It must also attach any document required by Cabinet Office regulations (*Article 27-3.2, FIEL*).

A bidder must, immediately after filing a registration statement of a public offer, send a copy of that statement to the issuing company and a stock exchange or securities dealers' association (*Article 27-3.4, FIEL*). A registration statement of a public offer is made public at the Local Finance Bureau and a stock exchange or securities dealers' association (*Article 27-14, FIEL*).

Preparing and delivering a public offer circular

A public bidder must prepare a public offer circular covering matters required in a registration statement of public offer (*see above, Filing of public offer registration statement*), and other matters prescribed by Cabinet Office regulations (*see Question 14*). Cabinet Office regulations also require that a public bidder deliver a public offer circular to any person who intends to sell shares (*Article 27-9, FIEL*).

Public offer period

The bidder must determine the period in which the shareholders' acceptances are to be filed. This must be between 20 and 60 business days from the issue of the public notice concerning the start of the public offer (*see above, Public notice of the start of a public offer*) (*Article 27-2.2, FIEL* and *Article 8. 1, COEF*).

As a general rule, during the offer period, a public bidder cannot purchase target shares other than by the public offer (*Article 27-5, FIEL*).

If a competing bid is made during the offer period, the public offer period can be extended until the final day of the competing public offer period (*Article 13.2.(2), COEF*). If the original public offer period (as stated in the public notice of the start of a public offer) is fewer than 30 business days, the target can require that the public offer period be extended to 30 business days (*Article 27-10. 3, FIEL* and *Article 9-3. 6, COEF*).

Expression of position on the bid by the target

The target must file with the Prime Minister its Position Report (*see Question 9*) within ten business days from the date of the public notice of the start of a public offer (*Article 27-10.1, FIEL*).

The target can pose questions to the bidder in the Position Report. If it does, the bidder must file with the Prime Minister a document setting out its response to the questions, as well as other matters required by Cabinet Office regulations. This must be done within five business days of receiving the Position Report (*Article 27-10.2 and 11, FIEL*).

Public notice of effects of a public offer

On the day after the last day of the offer period, the bidder must serve a public notice or make a public announcement regarding the number of shares applied for in the public offer, as well as other matters prescribed by Cabinet Office regulations (*Article 27-13.1, FIEL*).

In addition, on the date of the public notice or public announcement, the bidder must file with the Prime Minister a document reporting the content of this public notice or public announcement, as well as other matters prescribed by Cabinet Office regulations (*Article 27-13.2, FIEL*).

Delivery and other procedures for settlement of the purchase

A notice containing matters set out in Cabinet Office regulations, including the number of shares to be acquired by the bidder, must be sent without delay to an accepting shareholder after the offer period ends.

In addition, delivery and other procedures must be carried out without delay after the public offer period ends (*Article 27-2.5, FIEL* and *Article 8.5, COEF*).

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

These procedures and timetables apply regardless of whether a bid is recommended or hostile.

13. What conditions are usually attached to a takeover offer (in particular, is there a regulatory requirement that a certain percentage of the target's shares must be offered/bid)? Can an offer be made subject to the satisfaction of pre-conditions (and, if so, are there any restrictions on the content of these pre-conditions)?

A bidder must offer the same terms and conditions to all shareholders (uniform price and proportional distribution) (*Article 27-2.3, FIEL*). Conditions usually attached to a takeover offer are:

- A public bidder will not purchase:
  - any of the shares tendered by the shareholders, if the number of shares for sale is smaller than the number it originally planned to purchase (*Article 27-13.4, FIEL*); or
  - part or any of the tendered shares exceeding the number of shares it originally planned to purchase (*Article 27-13.4, FIEL*). (However, if the total voting ratio becomes two-thirds or more after the purchase, the bidder must make a mandatory offer for all shares (*see Question 16*).)
- A public offer can be withdrawn if an important change takes place in the business or property of the target, or if another event seriously hinders execution of the offer. This can only apply in situations set out in a cabinet order, including where (*Article 27-11.1, FIEL and Article 14, COEF*):
  - the target's decision-making body decides to carry out certain actions, including petitioning for bankruptcy, civil rehabilitation, corporate reorganisation or imposing or sustaining certain defence measures against hostile bids;
  - situations arise in relation to the target, including filing of a petition to suspend its business; and
  - a necessary permission from a government body is not obtained before the last day of the offer period, or where bankruptcy or other changes set out in a cabinet order take place in relation to the bidder.

Pre-conditions attached to the public offer are limited to the conditions stated above.

As a general rule, the bidder cannot make changes to the offer conditions that are disadvantageous to applicants for the offer. However, the bidder can reduce the purchase price, within certain limitations, where the target splits shares or makes a free issue of shares or share warrants, on condition that this is clearly stated in advance in both the public notice of the start of a public offer and the public offer registration statement.

This is allowed as, in such cases, the value of the shares falls and, if a reduction of the purchase price was not allowed, the bidder would suffer unexpected and unreasonable damages (*Article 27-6.1, FIEL* and *Article 13.1, COEF*).

14. What documents do the target's shareholders receive on a recommended and hostile bid? (Please briefly describe their purpose and main terms, and which party has responsibility for each document.)

A bidder must provide a public offer circular to shareholders who intend to accept a public offer and sell their shares (*Article 27-9, FIEL*) (*see Question 12, Preparing and delivering a public offer circular*).

A public offer circular aims to ensure:

- Proper allocation of consideration in a public offer.
- That shareholders have sufficient information to make investment decisions.

It is based on information in the registration statement of a public offer and is a means of direct disclosure.

The main terms required in a public offer circular are:

- The registration statement of the offer, excluding the name of any financial institution from which the public bidder is borrowing money.
- A statement that the offer is subject to Chapter 2-2 section 1 of the FIEL.
- A statement that the offer circular has been made according to Article 27-9 of the FIEL (*Article 24, Cabinet Office Regulation concerning Disclosure in a Public Offer by Entities other than the Issuer*).

The bidder must produce the public offer circular. If it contains a material misstatement or is not delivered, the bidder is subject to a penalty (*Articles 197-2(8) and 200(9), FIEL*).

15. Are there any requirements for a target's board to inform or consult its employees about the offer?

There are no requirements for a target's board to inform or consult its employees about the offer.

16. Is there a requirement to make a mandatory offer? If so, when does it arise?

If a party intends to purchase shares of public companies, this must be done by a public offer in certain cases (*Article 27-2.1, FIEL*) (*see Question 4*).

In addition, if, after the purchase, the total voting ratio becomes two-thirds or more, the bidder must make a mandatory offer for all shares (all types of voting shares) in the target and must purchase all shares for which it receives acceptances (*Article 27-13.4, FIEL* and *Article 14-2-2 and 8.5(3), COEF*).

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

CONSIDERATION

17. What form of consideration is commonly offered on a public takeover?

Generally, only cash is offered on a public takeover.

Legally, there is no special regulation of the form of consideration, so shares (including a bidder's own shares) can be used. However, there seems to have been no public offers in which shares have been used as consideration. The main reason for this is probably that shareholders cannot benefit from tax credits in a public offer (unlike, for example, a stock-for-stock exchange (*see Question 2*)).

If a bidder uses its own shares as consideration, continuous disclosure by the bidder is required under the FIEL. Foreign companies have difficulty with the time and cost of continuous disclosure in Japanese, although continuous disclosure in English has, since 2005, begun to be allowed under certain conditions (*Article 24.8 and 24-5.7, FIEL*).

If the bidder is a Japanese company, regulations apply concerning an in-kind capital contribution (*Article 207, Corporate Law*) and the issue of new shares to non-shareholders at a favourable issue price (*Articles 199.3 and 201.1, Corporate Law*). Therefore, it is difficult for Japanese companies to use their own shares as consideration in takeover bids.

18. Are there any regulations that provide for a minimum level of consideration? If so, please give details.

There are no regulations that provide for a minimum level of consideration.

19. Are there additional restrictions or requirements on the consideration that a foreign bidder can offer to shareholders? If so, please give details.

There are no additional restrictions or requirements on the consideration that a foreign bidder can offer to shareholders.

POST-BID

20. Can a bidder compulsorily purchase the shares of remaining minority shareholders? If so, please give details.

In mergers and stock-for-stock exchanges, an absorbing company or a company that will be a 100% parent company after the stock-for-stock exchange, can use not only its shares but also all kinds of assets (including money) as consideration for shares of the absorbed company or the company that will be a wholly-owned subsidiary after the stock-for-stock exchange (*Articles 749.1(2) and 768.1(2), Corporate Law*).

Therefore, a bidder can obtain the shares of remaining minority shareholders by using a merger or stock-for-stock exchange. In this case, the absorbed company or the company that will be a wholly owned subsidiary after the stock-for-stock exchange must publish in advance a document regarding the suitability of such consideration (*Article 782.1, Corporate Law* and *Articles 182.1(1) and 184.1(1), Enforcement Regulation of Corporate Law*).

21. If a bidder fails to obtain control of the target, are there any restrictions on it launching a new offer or buying shares in the target?

There are no restrictions on a bidder launching a new offer or buying shares in the target if a bidder fails to obtain control of the target by a public offer.

22. What action is required to de-list a company?

The company must undertake a transaction that satisfies the criteria for de-listing.

A stock-for-stock exchange or stock transfer can be used to de-list a company. If these cannot be used, the company can decrease the number of shareholders or increase the shareholding of the majority shareholders by purchasing its shares.

On the Tokyo Stock Exchange, companies are de-listed in any of the following ways (*Article 601, Security Listing Regulations*):

- The number of shareholders falls below 400 as of the last day of a fiscal year and does not return to that number within a year.
- The number of the units of the negotiable shares falls below 2,000 as of the last day of a fiscal year and does not return to that number within a year. Shares owned by any of the following are not negotiable: shareholders with a 10% or more shareholding ratio, officers of the issuing company, or the issuing company itself.
- The total market value of the negotiable shares falls below JPY500 million (about US$5.6 million) as of the last day of a fiscal year and does not return to that number within a year.
- The ratio of the negotiable shares divided by the number of all listed shares falls below 5% as of the last day of a fiscal year, and the company does not submit a scheduled plan of public offering, secondary offering or distribution.
- The company becomes a wholly owned subsidiary of another company by a stock-for-stock exchange or share transfer.
- The company issues new shares at a ratio of over 300% of the issued shares, or the company changes its controlling shareholder by the issue of shares, although there are exceptions in each case.

TARGET'S RESPONSE

23. What actions can a target's board take to defend a hostile bid (pre- and post-bid)?

Pre-bid

A target's board can take the following defensive actions, depending on the situation:

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

- Introducing a rights plan using share warrants (with discriminatory conditions, where only certain shareholders can execute the warrant and so on). This defence can be made by a resolution of a shareholders' meeting or a board meeting. In addition, it can be structured so that:
  - the company simply notifies in advance the possibility of using this defence and, after a bid is made, the company allots warrants to its shareholders; or
  - the company issues warrants to a trust bank (or special purpose company that entrusts the warrants to a trust bank), and the warrants are managed in a trust account. After a bid is made, the company can provide the warrants to shareholders (the trust bank distributes the warrants to shareholders). It is possible to issue warrants allowing the issuing company to compulsorily exchange the warrants for shares without the warrantholders' consent. In this way, the issuing company can defend against hostile bids rapidly and without the execution of warrants by warrantholders (*Article 236.1(7), Corporate Law*).
- Issuing shares that in effect can veto the approval of a merger or election or removal of directors (by requiring a resolution of a shareholders' meeting of the holders of such classes of shares on these matters) (*Article 108.1(8), Corporate Law*), or issuing shares with multiple voting rights to an amicable third party in advance (*Article 108.1(3), Corporate Law*).
- Amending the articles so that the company can impose restrictions on the requirement of shareholders' meeting approval regarding a merger or the removal of directors. In particular, the company can require approval of over two-thirds of the attending voting shares (the default requirement is approval of at least two-thirds of them) and/or approval by a certain number of shareholders, regardless of the number of shares held by such shareholders (*Article 309.2, Corporate Law*).

In practice, listed companies cannot use defensive measures if the Tokyo Stock Exchange believes that they unreasonably restrict the rights of shareholders or the exercise of these rights (*Article 601.1.(17), Security Listing Regulations of the Tokyo Stock Exchange*). The company will be de-listed if it introduces such a measure. The types of defensive measures that are effectively prohibited for listed companies include:

- Introduction of a rights plan, where the execution price of the share warrants is much lower than the market price and is given to shareholders as of the date of the introduction.
- Introduction of a rights plan, which the company cannot abolish and has no choice but to execute, even if a change in over half of the directors of the company has been resolved.
- A resolution or determination of an issuing class of shares with, in effect, power of veto (in other words, a resolution of a shareholders' meeting of the holders of such a class of shares is required) on important matters including election or removal of over half of the directors.

Post-bid

The following measures are considered defence measures but almost all of them have legal concerns and their effects are limited:

- **A significant increase in dividends.** This decreases a bidder's incentive to obtain control of the target by removing liquid assets.
- **Reduction of capital or fund reserves with compensation.** This has a similar effect as a significant increase in dividends.
- **Issuing new shares to an amicable third party.** This aims to increase the funds required to obtain control of the target, by increasing the number of shares issued. This is similar to the arrangement used in the Bull-Dog case (*see Question 3*), in which a company issues new share warrants to all shareholders with discriminatory conditions, so a hostile bidder cannot execute the warrant and so on.
- **Merger.** This increases the funds required to obtain control of the target by increasing the number of shares issued.
- **Forming a joint holding company with an amicable company by stock transfer, or acquiring such a company by stock-for-stock exchange.** This increases the funds required to obtain control of the target (or its successor company), by increasing the number of shares issued.

In relation to defensive measures used against hostile bids, in past decisions the Supreme Court of Japan has generally respected the judgment of the shareholders' meeting concerning the use of such measures.

TAX

24. Are any transfer duties payable on the sale of shares in a company that is incorporated and/or listed in your jurisdiction? Can payment of transfer duties be avoided?

Transfer tax is not payable on the sale of shares in a company incorporated in Japan. (Income tax or corporate tax and local tax calculated on capital gain (sale price minus acquisition cost) are imposed on the seller.)

OTHER REGULATORY RESTRICTIONS

25. Are any other regulatory approvals required, such as merger control and banking? If so, what is the effect of obtaining these approvals on the public offer timetable (for example, do the approvals delay the bid process, at what point in the timetable are they sought and so on)?

Merger control

Mergers, business acquisitions and share acquisitions that will substantially restrain competition in a particular market are prohibited under the Anti-monopoly Act (AMA). The AMA was recently amended in June 2009 and the amendments came into effect in January 2010. The AMA is enforced by the Japan Fair Trade Commission (JFTC). The JFTC sets out guidelines detailing those mergers, business acquisitions or share acquisitions that are considered to substantially restrain competition in a particular market (*Guidelines to Application of the Anti-monopoly Act Concerning Review of Business Combination (2004)*).

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

If mergers, business acquisitions or share acquisitions are assessed as restraining competition in such a manner, the JFTC can order the entity concerned to dispose of all or a part of its stock, to transfer a part of its business, or to take any other measure necessary to remedy the situation (*Article 17-2, AMA*).

In relation to mergers and business acquisitions that meet certain thresholds, the parties concerned must file a pre-merger notification or a pre-acquisition notification with the JFTC, and the parties cannot complete the transaction until 30 days has passed from the date that the JFTC accepted the notification (*Articles 15 and 16, AMA*). Under the AMA, this also applies to share acquisitions that meet certain thresholds (*Article 10, AMA*). This applies not only to a share purchase transaction (including a tender offer), but also to the issuance of shares for subscription and a share-for-share exchange transaction.

In the case of a public offer, if the 30-day waiting period has not ended by the last day of the public offer period, a public offer can be withdrawn because a necessary permission from a government body has not been obtained. This is on the condition that this withdrawal is expressly provided for in the tender offer filing and public notice (*see Question 13*). However, the FSA has announced that the bidder must arrange for the waiting period to end by the last day of the public offer period when it determines the:

- Start date of the public offer.
- Filing date of the pre-acquisition notification.
- Period of the public offer.

If the share acquisition is viewed as substantially restraining competition in a particular market, the JFTC may order the bidder to dispose of all or a part of its stock. Therefore, a bidder intending to make a public offer that may impact on competition, when appropriate, may wish to consult with the JFTC and confirm that the share acquisition will not be assessed as substantially restraining competition, before issuing a public notice of the start of a public offer (*see Question 12*).

Since 2004, the JFTC's Guidelines have required, in addition to a market share analysis, a review of the transaction's Herfindahl-Hirschman Index (HHI) to determine whether a merger, business acquisition or share acquisition substantially restrains competition in a particular market. In 2007, the JFTC's Guidelines were revised to define a safe harbour based on the HHI, where it is reasonably believed that the transaction will not substantially restrain competition. Case-by-case reviews are not required of transactions that fall within the safe harbour.

Regulation of bank shareholders

An entity that intends to hold more than a certain percentage (generally 20%) of voting rights in a bank must obtain the approval of the Commissioner of the FSA (*Article 2.9, 52-9.1 and 59.1, Banking Law*).

Approval must be obtained by, at the latest, settlement of the purchase (*see Question 12*). If the entity concerned does not do this, it is subject to administrative fines (*Article 65(14), Banking Law*).

THE REGULATORY AUTHORITY

Financial Services Agency (FSA)

Head. Mr Katsunori Mikuniya (Commissioner)

Address. The Central Common Government Offices
No 7
3-1-1 Kasumigaseki
Chiyoda-ku
Tokyo 100-8967
Japan
T +81 3 3506 6000 (main switchboard)
F +81 3 3506 6266
E *www.fsa.go.jp/opinion*
W *www.fsa.go.jp/index.html*

Main area of responsibility. The FSA's main areas of responsibility are:

- The planning of the securities markets' system.
- Collecting, analysing and investigating materials and information concerning securities transactions.
- Supervising securities companies.

Contact for queries. Corporate Accounting and Disclosure Division, Planning and Co-ordination Bureau.

Obtaining information. See website above.

It takes at least one month from the application date to obtain approval (or two months for certain banks designated by the Minister of the FSA) (*Article 40, Enforcement Regulations of the Banking Law*). For practical reasons, the entity should:

- Consult with the FSA before issuing the public notice of the start of a public offer (*see Question 12*).
- Apply for approval in the early stages of the transaction.

Regulation of insurance companies' shareholders

Regulations similar to those imposed on banks are imposed on shareholders of insurance companies (*Article 271-10.1, Insurance Business Law*) (*see above, Regulation of bank shareholders*).

26. Are there restrictions on foreign ownership of shares (generally and/or in specific sectors)? If so, what approvals are required for foreign ownership and from whom are they obtained?

If a foreign company intends to obtain 10% or more of the shares in a company operating in certain regulated industries, it must give prior notification to the Minister of Finance and the minister in charge of the relevant industry (*Articles 26.2.(3) and 27, Foreign Exchange and Foreign Trade Law*). Such industries include aircraft, weapons, atomic energy and space development.

Where prior notification is necessary, the foreign company cannot generally invest until 30 days after the date on which the notification was received (this can be extended to up to five months by the

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

relevant Ministers). The Minister of Finance and minister in charge of the relevant industry can recommend that the foreign company alter the scope of the investment or suspend it on national security grounds (*Article 27, Foreign Exchange and Foreign Trade Law* and *Article 3, Cabinet Order Concerning Direct Inward Investment*). Where prior notification is unnecessary, if a foreign company intends to obtain 10% or more of the shares in a listed company, it must, in principle, notify the Minister of Finance and the minister in charge of the relevant industry by the fifteenth of the month following the month in which the acquisition took place.

In relation to the Nippon Telegraph and Telephone Corporation (NTT), broadcasting companies and air transport companies, there are specific regulations regarding the ownership of shares by foreign entities.

The NTT Law provides that foreign entities cannot hold one-third or more of the voting rights in NTT (*Article 6, Nippon Telegraph and Telephone Corporation Law*).

Under the Radio Law, a radio station licence (which is necessary for broadcasting) cannot be granted to a company where the voting rights of foreign entities of the company reach or exceed one-fifth. Accordingly, a broadcasting company can refuse to register shares held by foreign entities in these circumstances (*Article 52-8, Broadcast Law*).

Under the Aviation Law, approval of the Minister of the Land, Infrastructure, Transport and Tourism Ministry (which is necessary for air transport business) cannot be granted to a company where the voting rights of foreign entities of the company reach or exceed one-third (*Articles 4.1(4) and 101, Aviation Law*). Accordingly, an air transport company can refuse to register shares held by foreign entities in these circumstances (*Article 120-2, Aviation Law*).

27. Are there any restrictions on repatriation of profits or exchange control rules for foreign companies? If so, please give details.

If there is a repatriation of profits over JPY30 million (about US$0.3 million), a report on payment or receipt of payment must be submitted after the event (*Article 55, Foreign Exchange and Foreign Trade Law, Article 18-4.1, Cabinet Order concerning Foreign Exchange and Foreign Trade* and *Article 1, Ministerial Order concerning Report of Foreign Exchange and Foreign Trade*).

The department to which the report must be submitted and the relevant time limits vary, depending on the methods of payment and so on. It is therefore advisable for an entity to contact and consult with the Bank of Japan on a case-by-case basis.

28. Following the announcement of the offer, are there any restrictions or disclosure requirements imposed on persons (whether or not parties to the bid or their associates) who deal in securities of the parties to the bid?

During a public offer period, a bidder generally cannot purchase target shares by means other than a public offer (*Article 27-5, FIEL*) (*see Question 12*).

If, during the period in which another party's public offer is made, a party whose total voting ratio before the purchase exceeds one-third intends to purchase over 5% of the voting shares, it must do so through a public offer (*see Question 4, Regulation of public takeovers*).

REFORM

29. Please summarise any proposals for the reform of takeover regulation in your jurisdiction.

The regulations governing public offers were substantially amended in 2006. No further amendment is definitively planned at this stage, although several possible changes are being discussed. These proposals include:

- Bringing the purchase of shares on the stock exchange market within the scope of purchases requiring a public offer. This would mean that, if a party intends to obtain a certain threshold percentage of voting shares within a specified period, and the total voting ratio would exceed one-third after obtaining such shares, the party would have to obtain those shares by way of a public offer. This proposal is intended to protect minority shareholders from the sudden and unexpected appearance of a controlling shareholder.
- In cases where the number of total sellers is at or below a certain number, the removal of the requirement that the purchase be made via a public offer, regardless of the purchaser's total voting ratio after the purchase (*see Question 4, Regulation of public takeovers*). This proposal is intended to make corporate acquisitions easier. It is based on the theory that, in cases falling within such circumstances, the sellers of the shares generally have sufficient information to make an informed decision as to whether to sell and there is little need to have the bidder go to the trouble of putting together a public offer.

CONTRIBUTOR DETAILS

Masakazu Iwakura and Tomohiro Takagi
Nishimura & Asahi
T +81 3 5562 8500
F +81 3 5561 9711
E *info@jurists.co.jp*
W *www.jurists.co.jp/en*

© This article was first published in the PLC Cross-border Mergers and Acquisitions Handbook 2010/11 and is reproduced with the permission of the publisher, Practical Law Company. For further information or to obtain copies please contact iain.plummer@practicallaw.com, or visit www.practicallaw.com/acquisitionshandbook

NISHIMURA&ASAHI

Our commitment to professionalism and client service has facilitated the firm in becoming one of Japan's leading providers of domestic and international corporate and business legal services.

Acquisition Finance, Administrative Disputes, Antitrust, Asset Finance, Asset Management, Assistance to Administrative Organizations, Banking, Capital Markets, Civil & Commercial Disputes, Compliance, Corporate Crisis Management, Education and Professional Activities, General Corporate, Insurance, International Trade, International Transactions, Investment Trusts, IP Disputes, IP Licenses, Labor Law, M&A, PFI/Project Finance, Real Estate/Environmental, Restructuring/Insolvency, Specialized Disputes, Start-up Businesses, Structured Finance/Securitization, Tax, Tax Disputes, Telecommunications/Media, Transnational Dispute Settlement, Trusts & Estates, Venture Capital/IP Finance

Ark Mori Building
1-12-32 Akasaka, Minato-ku, Tokyo 107-6029 JAPAN
Tel: 81-3-5562-8500
Fax: 81-3-5561-9711/12/13/14
URL: www.jurists.co.jp Email: info@jurists.co.jp

Contact Person: Mr. Akira Kosugi (Managing Partner)
Total Number of Attorneys: 440
Languages Spoken: Japanese, English, Chinese (Mandarin) and French