

Expansion of Business Sectors Subject to Investment Screening in Japan for the Purpose of Securing Stable Supply Chains

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On March 9, 2023, the Ministry of Finance and competent ministries released, among other documents, draft amendments to the public notices concerning the Japanese government security screening system for certain investments and other activities made or conducted by foreign investors, whereby subject business sectors will be added (“**Draft Public Notices**”). The public comment procedure for the Draft Public Notices has begun and will end on April 7.¹ Accordingly, this Newsletter provides a brief outline of the Draft Public Notices.

1. Inward Direct Investment Screening System and Amendments to Business Sectors Subject to the Screening

While the basic principle of the Foreign Exchange and Foreign Trade Act (the “**FEFTA**”) is free investment, the FEFTA requires, from the viewpoint of implementing minimum control and coordination based on the national security, that prior-notification be filed with the Ministry of Finance and competent ministries and agencies for the relevant business when a foreign investor (e.g., non-resident, foreign corporation, company in which 50% or more of the voting rights are held by foreign capital, etc.) makes investment or the like (e.g., acquiring 1% or more of voting rights of a listed company, acquiring a share of an unlisted company, etc.) in a company that belongs to certain business sectors (“**Designated Business Sectors**”).² The Ministry of Finance and competent ministries and agencies for the relevant business implement screening of investments or the like for which prior-notification was filed by foreign investors and, if they determine that there is a risk of national security being affected, may take rectification measures towards the relevant foreign investor, such as issuing a recommendation or order of modification or discontinuance. Foreign investors may sometimes be exempted from the prior-notification mentioned above (“**Prior-Notification Exemption**”³) in cases of investment through stock acquisition that satisfy certain requirements, such as neither the foreign investors themselves nor their related persons assuming officer positions or accessing non-public technical information. However, as a general rule, the Prior-Notification Exemption cannot be used for investment in certain business sectors designated from among the Designated Business Sectors as being highly likely to damage national security (“**Core Business Sectors**”).⁴

¹ <https://public-comment.e-gov.go.jp/servlet/Public?CLASSNAME=PCMMSTDETAIL&id=395122313&Mode=0>

² Article 26, paragraph (2), Article 27, paragraph (1), Article 26, paragraph (3), and Article 28, paragraph (1) of the FEFTA.

³ Article 27-2, paragraph (1) and Article 28-2, paragraph (1) of the FEFTA.

⁴ Article 27-2, paragraph (1) and Article 28-2, paragraph (1) of the FEFTA; Article 3-2, paragraph (2), item (iii) and Article 4-3, paragraph (2), item (i) of the Cabinet Order on Inward Direct Investment.

Since around the time when the FEFTA was amended from 2019 to 2020 (Act Partially Amending the Foreign Exchange and Foreign Trade Act (Act No. 60 of November 29, 2019), promulgated on November 29, 2019 and put into force on May 8, 2020),⁵ the Designated Business Sectors and the Core Business Sectors subject to investment screening under the FEFTA have been amended successively through amendments to the relevant public notices, as shown in the table below.

Amendments to Public Notices	Details of Amendments
August 2019	Cyber security-related business sectors (e.g., software IT, integrated circuit, etc.) were added to the Designated Business Sectors.
June 2020	Manufacturing of pharmaceuticals for infectious diseases and manufacturing of specially-controlled medical devices were added to the Designated Business Sectors and the Core Business Sectors.
October 2021	Among other business sectors, metal mining for important mineral resources, such as rare earths, and construction to develop port and harbour facilities in the specified isolated islands ⁶ were added to the Designated Business Sectors and the Core Business Sectors.

According to the explanatory material outlining the Draft Public Notices,⁷ “in response to the recent designation of “Specially Designated Critical Commodities”, which are eligible for receiving support for securing stable supply under the Economic Security Promotion Act⁸, as a result of the consideration from the perspective of the FEFTA,” the Draft Public Notices add some business sectors subject to the screening “in order to secure stable supply chains and address the risk of technology leakage and diversion of commercial technologies into military use, etc.” The explanatory material also states that as a result of addition to the Core Business Sectors by the Draft Public Notices, “Specially Designated Critical Commodities” under the Economic Security Promotion Act will be fully covered as Core Business Sectors. Therefore, the addition of business sectors subject to the screening (Designated Business Sectors and Core Business Sectors) by the Draft Public Notices seems to be essentially designed to be consistent with measures concerning supply chain resilience based on the Economic Security Promotion Act (i.e., Chapter 2, systems to ensure stable supply of Specially Designated Critical Commodities).

After the Economic Security Promotion Act was enacted and promulgated in May last year, the portions of that Act concerning supply chain resilience systems were put into force the following August. After that, in December last year, the eleven types of commodities specified below were designated by Cabinet Order as

⁵ For details of the amendment, please see, for example, “Rules and Regulations of the Foreign Exchange and Foreign Trade Act” dated April 24, 2020, which was released by the Ministry of Finance (https://www.mof.go.jp/english/policy/international_policy/fdi/kanrenshiryoku01_20200424.pdf).

⁶ Isolated islands far away from the mainland that are important as a base of activities in light of the existence of natural resources among other factors and designated by Cabinet Order under the “Act on Reservation of Low-water Line and Development of Base Facilities for Facilitating the Reservation and Use of Exclusive Economic Zone and the Continental Shelf” as particularly having need for development of facilities used as a base of activities (i.e., *Okinotorishima* and *Minamitorishima*).

⁷ https://www.mof.go.jp/english/policy/international_policy/fdi/20230309.pdf

⁸ Act on the Promotion of National Security through Integrated Economic Measures

commodities that satisfy the predetermined requirements⁹ under the Economic Security Promotion Act and are eligible for the government support measures (“**Specially Designated Critical Commodities**”) (see Article 7 of the Economic Security Promotion Act; Article 1 of the Enforcement Order of the Act on the Promotion of National Security through Integrated Economic Measures; and Chapter 3 of the Basic Guidelines for Ensuring Stable Supply of Specially Designated Critical Commodities).¹⁰

Before the designation of the Specially Designated Critical Commodities, the government conducted supply chain analysis and research, closely examined the applicability of the legal requirements. Based on the results of the foregoing, the Specially Designated Critical Commodities were designated. Currently, plans to ensure supply of each Specially Designated Critical Commodity are being submitted in accordance with the action policy for each type of commodity established by the competent ministry or agency for that type of commodity.

(i) Antimicrobial preparations, (ii) fertilizers, (iii) permanent magnets, (iv) machine tools and industrial robots, (v) aircraft parts (comprising aircraft engines and airframes), **(vi) semiconductors** (semiconductor devices and integrated circuits), **(vii) storage batteries, (viii) cloud programs, (ix) combustible natural gas (LNG), (x) metal minerals,¹¹ and (xi) marine parts** (marine engines, navigational tools, and propellers)

2. Business Sectors Added by the Draft Public Notices

The business sectors added to the Designated Business Sectors and the Core Business Sectors by the Draft Public Notices are the 12 business sectors specified below. As stated above, basically, the business sectors added are related to commodities designated as Specially Designated Critical Commodities. The additions basically were made to both the Designated Business Sectors and the Core Business Sectors without making a distinction between inward direct investment and specified acquisition (acquiring shares of an unlisted company from a foreign investor). Although they are not designated as Specially Designated Critical Commodities, business sectors concerning metal 3D printers have been added to the Designated Business Sectors and the Core Business Sectors. Furthermore, it has been clarified that manufacturing of drones (unmanned aerial vehicles) are covered by aircraft manufacturing (which is a Core Business Sector), which was not necessarily clear before. Some petroleum-related business sectors (crude oil and natural gas mining, petroleum refining, and petroleum storage) and manufacturing of antimicrobial preparations, which were not included in the Designated Business Sectors or the Core Business Sectors for specified acquisition before, have been added to the Designated Business Sectors and the Core Business Sectors for specified acquisition.

⁹ Four requirements need to be satisfied: commodities must (i) be indispensable for the survival of the people or widely depended on by the lives or economic activities of the people, (ii) be or may be excessively dependent on external parties, (iii) have a certain probability of experiencing supply disruption, etc., due to actions taken by external parties, and (iv) necessitate the measures under this system (Article 7 of the Economic Security Promotion Act).

¹⁰ For the Economic Security Promotion Act, see also N&A Newsletter ([Update to Economic Security Promotion Act: Designation of supported materials \(specified critical materials\) in relation to supply chain resilience](#))

¹¹ They are limited to manganese, nickel, chromium, tungsten, molybdenum, cobalt, niobium, tantalum, antimony, lithium, boron, titanium, vanadium, strontium, rare earth metals, platinum group metals, beryllium, gallium, germanium, selenium, rubidium, zirconium, indium, tellurium, cesium, barium, hafnium, rhenium, thallium, bismuth, graphite, fluorine, magnesium, silicon, and phosphorus.

No.	Business Sector	Inward Direct Investment		Specified Acquisition		Specially Designated Critical Commodities
		Designated Business Sector	Core Business Sector	Designated Business Sector	Core Business Sector	
1.	Refining of metal minerals	✓	✓	✓	✓	✓
2.	Semiconductor-related manufacturing <ul style="list-style-type: none"> ● Manufacturing of production devices for semiconductors ● Manufacturing of semiconductor devices (excluding photoelectric conversion elements) ● Manufacturing of electric circuit boards ● Manufacturing of semiconductor parts and materials specially designed for manufacturing of semiconductor devices or integrated circuits ● Manufacturing of helium and rare gases for use in manufacturing ● Manufacturing of phosphorus compounds and hydrofluoric acid for use in manufacturing 	✓	✓	✓	✓	✓
3.	Related to metal 3D printers <ul style="list-style-type: none"> ● Manufacturing of metal 3D printer devices ● Manufacturing of powdered metals and metal alloys specially designed as a material for metal 3D printer devices 	✓	✓	✓	✓	—
4.	Related to NC metal cutting machine tools¹² and industrial robots¹³ <ul style="list-style-type: none"> ● Manufacturing of NC metal cutting machine tools and industrial robots ● Manufacturing of speed reducers, servomechanisms, numerically controlled equipment, and programmable logic controllers used for manufacturing and repairs ● Software business concerning programs specially designed to use NC metal cutting machine tools and 	✓	✓	✓	✓	✓

¹² Numerically controlled metal cutting machine tools.

¹³ Industrial robots that are mainly used for manufacturing of industrial goods.

No.	Business Sector	Inward Direct Investment		Specified Acquisition		Specially Designated Critical Commodities
		Designated Business Sector	Core Business Sector	Designated Business Sector	Core Business Sector	
	industrial robots ¹⁴					
5.	Related to storage batteries (lithium-ion storage batteries for automotive¹⁵ and stationary applications) <ul style="list-style-type: none"> ● Manufacturing of storage batteries ● Manufacturing of parts, materials, or devices specially designed for use in manufacturing 	✓	✓	✓	✓	✓
6.	Related to permanent magnets (for weapons, electric motors, electric generators, and medical machines and equipment) <ul style="list-style-type: none"> ● Manufacturing of permanent magnets ● Manufacturing of materials specially designed for use in manufacturing 	✓	✓	✓	✓	✓
7.	Manufacturing of marine parts (those listed below) <ul style="list-style-type: none"> ● Diesel engine (2-cycle with a maximum continuous output of 735 kilowatt or more) and crankshafts ● Sonar ● Propeller (with a diameter exceeding 1,600mm) 	✓	✓	✓	✓	✓
8.	Importation of fertilizers (the amount of the items below imported per year is 1,000 tons or more) <ul style="list-style-type: none"> ● Potassium chloride (for use as fertilizers) ● Diammonium hydrogenphosphate, ammonium dihydrogenphosphate, etc. (for use as fertilizers) 	✓	✓	✓	✓	✓
9.	Manufacturing of antimicrobial preparations <ul style="list-style-type: none"> ● Manufacturing of pharmaceuticals with certain¹⁶ active components against 	— * Already designated as	— * Already designated as	✓	✓	✓

¹⁴ With respect to the Designated Business Sector (Inward Direct Investment), this business sectors does not seem to be newly designated; however, it seems to be covered by the software business already included in the Designated Business Sectors.

¹⁵ Limited to use as a driving power source.

¹⁶ Ampicillin sodium and sulbactam sodium, piperacillin sodium and tazobactam sodium, ceftazolin sodium, or cefmetazole sodium.

No.	Business Sector	Inward Direct Investment		Specified Acquisition		Specially Designated Critical Commodities
		Designated Business Sector	Core Business Sector	Designated Business Sector	Core Business Sector	
	pathogens ● Intermediates of the pharmaceuticals above	“Manufacturing of pharmaceuticals against pathogens”	“Manufacturing of pharmaceuticals against pathogens”			
10.	Wholesale of natural gas	— *Already designated as “Petroleum wholesale”	✓	✓	✓	✓ *Regarding combustible natural gas
11.	Crude oil mining, natural gas mining, petroleum refining, petroleum storage	— *Already designated	— *Already designated	✓	✓	✓ *Regarding combustible natural gas
12.	Manufacturing of and repair business concerning unmanned aerial vehicles (drones)	✓ *Clarified	✓ *Clarified	✓ *Clarified	✓ *Clarified	—

3. Future Schedule and Outlook

The Basic Policy on Economic and Fiscal Management and Reform 2022 (Cabinet Decision dated June 7)¹⁷ states as the government policy that the government will consider what businesses should be designated as business subject to the mandatory prior notification. In addition, another basic policy established under the Economic Security Promotion Act states that integrity and consistency will be ensured among economic measures to ensure security (e.g., Chapter 4, (2) and (4) of that basic policy). Considering the foregoing, it is not surprising that, in relation to the Specially Designated Critical Commodities entitled to support measures under the Economic Security Promotion Act, another system—the screening system under the FEFTA—be reconsidered in the form of adding business sectors subject to the screening. What we should note is that the integrity and consistency among measures concerning economic security seem to have become increasingly important. It seems that consistency between measures has been maintained in the context of export control and investment screening. For example, in the framework of the FEFTA, with respect to the goods and technologies subject to the export control, business concerning such goods and technology has been subject to investment screening. In the future, the Designated Business Sectors may be reconsidered

¹⁷ https://www5.cao.go.jp/keizai-shimon/kaigi/cabinet/2022/2022_basicpolicies_en.pdf

again if consistency is required between economic measures to ensure security, including those under the Economic Security Promotion Act, and investment screening measures.¹⁸

The addition of business sectors by the Draft Public Notices can be described as broad-ranging but not infinite, because the designation of the Designated Business Sectors seems to be consistent with the action policies established for each type of Specially Designated Critical Commodities by the ministries and agencies responsible for the relevant commodities under the Economic Security Promotion Act. For example, in the action policy concerning fertilizers (the “**Action Policy**”), for the purpose of “ensuring stable supply of fertilizers by newly building storage systems for ammonium phosphate and potassium chloride, regarding which a tight supply-demand balance is highly likely to make it difficult to produce fertilizers,” the government’s action for support is limited to that concerning ammonium phosphate and potassium chloride; and the scope of addition by the Draft Public Notices stands on the foregoing. Furthermore, it seems that import business operators with stock functions, rather than fertilizer manufacturers, are covered by the Designated Business Sectors and the Core Business Sectors in light of (a) the fact that these raw materials of fertilizers are dependent on import and (b) the supply chain structure of fertilizers, i.e., “import business operators sometimes have a certain stock function for raw material inventories because procurement of raw materials for fertilizers mainly takes the form of fertilizer manufacturers making requests (placing orders) to import business operators for procurement of such amount of raw materials as necessary to manufacture fertilizers for the time being based on the manufacturers’ manufacturing plans” (Chapter 1, Section 1, (6) of the Action Policy).

From among the addition of business sectors by the Draft Public Notices, what interests us is the addition to the Designated Business Sectors and the Core Business Sectors for the purpose of protecting a semiconductor supply chain. To be more specific, the Draft Public Notices add manufacturing in fields where Japan has a competitive edge, such as materials and production devices for semiconductors, irrespective of specs, and a wide range of semiconductor-related business sectors such as manufacturing of semiconductor devices and electronic circuit boards, on top of (a) semiconductor-related business, including manufacturing of integrated circuits, manufacturing of semiconductor memory media, and manufacturing of electronic circuit mounting boards, having been added through the addition of cyber security-related business sectors to the Designated Business Sectors in August 2019 and (b) manufacturing of and other business concerning semiconductor production devices, resists, silicon wafers, etc., with certain specs, already contained in the Designated Business Sectors due to the fact that they are subject to security trade controls.¹⁹ Consequently, the Draft Public Notices seem to identify most of the businesses composing the semiconductor-related supply chain as business sectors subject to investment screening. Strategic acquisitions of semiconductor-related businesses by foreign investors are expected to be carefully screened, with respect to almost every business category.

April 7 is the deadline for opinions in the Draft Public Notices public comment procedure. At present, a specific application time for the Public Notices has not been determined. For foreign investors that consider investing in companies belonging to the newly added Designated Business Sectors or Core Business Sectors, the time of closing may be affected by notification screening under the FEFTA, depending on the

¹⁸ The U.S. Executive Order (EO 14083) signed by President Biden on September 15, 2022 made it clear that maintenance of supply chain resilience is taken into account by the CFIUS (Committee on Foreign Investment in the United States) in its screening of investment in the U.S.. Thus, consistency between economic security measures has been achieved.

¹⁹ See Appended Table 1, item (v) of “Public Notice Specifying Business Types to Be Specified by the Minister of Finance and the Competent Minister for the Business Pursuant to the Provisions of Article 3, Paragraph (3) of the Order on Inward Direct Investment” and Appended Table 1, item 7 of the “Export Trade Control Order.”

time of the relevant transaction. Further, in cases where a foreign investor appoints itself or its related person as a director or statutory auditor, if there is a possibility that voting in favor of the appointment may be conducted after the day on which a 30-day period has elapsed since the date of application of the Draft Public Notices, notification screening under the FEFTA will need to be taken into account in terms of scheduling.

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