

Modification to the Legal Framework Governing Rights Offering in Japan

On March 30, 2011, we issued a newsletter¹, which outlined a report issued by the Japanese Financial Services Agency (“FSA”) on the potential modifications to the regulations governing the allotment of stock acquisition rights to shareholders without consideration (“Rights Offering”) (the “Report on Modifications”).

Following this newsletter, on May 17, 2011, the amendment bill of the Financial Instruments and Exchange Act (“Amended FIEA”) relating to Rights Offerings was enacted in the Diet.² Further, on November 4, 2011, the FSA published proposed draft amendments to government ordinances, cabinet office ordinances and guidelines regarding the disclosure requirements and other requirements governing Rights Offering (the “Amendments to the Ordinances and Guidelines”).³

Although the proposed Amendments to the Ordinances and Guidelines have been subject to public comment until December 5, 2011 and as such may change, the purpose of the Amended FIEA will not change. In essence, the Amended FIEA and the Amendments to the Ordinances and Guidelines will implement changes in accordance with the proposals made in the Report on Modifications through both encouraging the use of Rights Offering and its effective regulation. The Amended FIEA and the Amendments to the Ordinances and Guidelines are scheduled to come into effect on April 1, 2012.

The following is an overview of the contents and the purpose of the Amended FIEA, the proposed Amendments to the Ordinances and Guidelines and the Report on the Equal Treatment Rule among Shareholders (as defined below).

I. Amendment to FIEA and Relevant Ordinances

I.1. Matters Regarding Disclosure Documents

I.1.A. Reduced burden regarding the delivery of prospectuses

The Amended FIEA and Amendments to the Ordinances and Guidelines will allow an issuer conducting a Rights Offering to be released from the obligation of delivering a prospectuses to its existing shareholders where (i) the stock acquisition rights to be offered in a Rights Offering are or will be listed on a stock exchange in Japan, (ii) the issuer files a Securities Registration Statement (“SRS”) in connection with the Rights Offering and discloses the SRS through the EDINET system, and (iii) the issuer provides constructive notice to shareholders through daily newspaper advertisements which inform the public of (a) the web address of EDINET, (b) the day on which the SRS was filed and (c) the contact address of the issuer.

¹ http://www.amt-law.com/pdf/bulletins2_pdf/110330.pdf

² <http://www.fsa.go.jp/common/diet/index.html>

³ <http://www.fsa.go.jp/news/23/syouken/20111104-1.html>

I.1.B. Reduction of the burden of amendment to the SRS

Under the regulations before the contemplated amendment, if, after filing an initial SRS in connection with a Rights Offering, the issuer files any continuous disclosure documents (such as an annual securities report or a quarterly report), the issuer must file an amendment to the SRS for the purpose of incorporating by reference the newly filed continuous disclosure document. However, under the proposed Amendments to the Ordinances and Guidelines, if the scheduled time of filing of the relevant continuous disclosure document is stated in the initial SRS, then the amended SRS will no longer be required.

I.2. Matters regarding takeover bids and large shareholding reports

I.2.A. Application of the takeover bid regulations and large shareholding report regulations at the time of exercising stock acquisition rights

Under the proposed Amendments to the Ordinances and Guidelines, in cases where so-called “commitment” type Rights Offerings⁴ are conducted and where the period from the day when the stock acquisition rights are issued and the last day of the exercising period of the stock acquisition rights is within two months, the takeover bid regulations and the duty to file large shareholding reports will be applied at the time of exercising stock acquisition rights and not at the time of allotment of such rights to shareholders.

I.2.B. The underwriter’s exemption period from the takeover bid regulations and large shareholding report

In principle, those who acquire a listed company’s equity securities such as shares and stock acquisition rights over a prescribed shareholding ratio threshold are subject to the takeover bid regulations and are required to file large shareholding reports. However, as the underwriters of commitment type Rights Offerings inevitably acquire and hold a considerable number of unexercised stock acquisition rights, it has been pointed out that a sufficient exemption period which allows the underwriters of commitment type Rights Offering to hold the stock acquisition rights is essential. Under the proposed Amendments to the Ordinances and Guidelines, stock acquisition rights which have been acquired by underwriters according to its commitment but which will not be held for longer than 60 days (in the case of the takeover bid regulation) or 5 business days (in the case of large shareholding reports) following the day when the underwriter acquires the stock acquisition rights, will be excluded for the purpose of calculating the underwriters’ shareholding ratio under the takeover bid regulations and the large shareholding reports requirement.

I.3. Matters regarding the Insider Trading Regulations

⁴ A type of Rights Offering which involves a firm commitment by an underwriter (*i.e.*, securities company) to acquire all unexercised stock acquisition rights (such underwriter will thereafter exercise such stock acquisition rights and sell the shares to be acquired upon such exercise through the secondary market).

I.3.A. Clarification regarding the scope of the Material Fact

The Amended FIEA clearly stipulates that determination regarding the allotment of stock acquisition rights to shareholders without consideration is included in the material fact⁵ in terms of the insider trading regulations in Japan.

I.3.B. Establishment of the minor exception regarding Rights Offering

The proposed Amendments to the Ordinances and Guidelines provide that, a corporate decision to allot stock acquisition rights to the existing shareholders without consideration will not be considered as a “material fact” and therefore the insider trading regulations will not apply, where (i) the amount to be paid in exercising stock acquisition rights is less than JPY 100 million, and (ii) the ratio of the number of shares to be issued by exercising the stock acquisition rights to be allotted to the number of outstanding shares is less than ten per cent.

I.3.C. Exemption in the case of acquisition or sale of stock acquisition rights without arbitrariness by the issuer

Under the Proposed New Rules, the insider trading regulations shall not apply to the case where an issuer conducting a commitment-type Rights Offering either (a) acquires unexercised stock acquisition rights from investors or (b) sells such acquired stock acquisition rights to an underwriter, in accordance with the Rights Offering plan which was determined and published before becoming aware of a material fact.

I.4. Regulation on solicitation of exercising stock acquisition rights

I.4.A. Expansion of the scope of “Underwriting of Securities”

Under the Amended FIEA, a contract which stipulates the acquisition of all unexercised stock acquisition rights or the exercise of stock acquisition rights and which constitutes an essential part of commitment type Rights Offering will be included in the definition of “Underwriting of Securities”.

I.4.B. Regulations on solicitation of stock acquisition rights

The proposed Amendments to the Ordinances and Guidelines state that underwriters (*e.g.*, securities companies) shall not conduct any of the following acts:

- (i) provide a Rights Offering investor with false information in the course of solicitation to exercise his/her stock acquisition rights; or
- (ii) provide a Rights Offering investor with conclusive evaluations on uncertain matters or with information that misleads him/her into believing the certainty of such matters, in the course of solicitation to exercise his/her stock acquisition rights.

⁵ A certain fact which if a person becomes aware of, that person will be subject to the insider trading regulations and is prohibited from trading certain shares, etc. in a company prior to or at the time of disclosure of the fact (*e.g.*, the determination of merger).

I.5. Inclusion of foreign stock acquisition rights

Under the proposed Amendments to the Ordinances and Guidelines, securities issued by a non-Japanese company, which are of similar nature to stock acquisition rights in Japan, shall be included within the definition of “stock acquisition rights”. Accordingly, the Amended FIEA and the Amendments to the Ordinances and Guidelines would also be applicable to Rights Offerings by non-Japanese companies using securities similar to Japanese stock acquisition rights.

1.6. Effective Date

As stated above, the Amended FIEA and the Amendments to the Ordinances and Guidelines are scheduled to come into effect on April 1, 2012.

II. Report on the equal treatment rule among shareholders in Japan and foreign securities regulations regarding Rights Offering

On September 17, the FSA issued a report titled “The Issue between the Equal Treatment Rule among Shareholders in Japan and Foreign Securities Regulations regarding Rights Offering.” (the “**Report on the Equal Treatment Rule among Shareholders**”)⁶.

The Report on the Equal Treatment Rule among Shareholders argues that imposing restrictions on the exercise of stock acquisition rights on shareholders who reside in certain foreign countries, in order to avoid excessive application of foreign securities regulations, should not be construed as treating shareholders unequally and should not violate the “equal treatment rule among shareholders” under the Companies Act of Japan.

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⁶ <http://www.fsa.go.jp/en/news/2011/20111006-1.html>

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