M&A Update

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The Personal Information Protection Act and its Effect on Mergers & Acquisitions

The *Personal Information Protection Act* (PIPA), which came into full effect on April 1 2005, presents some new challenges in respect to due diligence and subsequent phases of mergers and acquisitions.

Provisions of the PIPA

Personal information is information that makes it possible, on its own or in conjunction with other information, to identify a particular individual. The PIPA controls the acquisition, as well as the handling and dissemination of this personal information.

Entities handling personal information (information handlers) must, at the time of acquisition or shortly thereafter, disclose the purposes for which the personal information will be used to the person identifiable by that personal information (the protected principal - Article 18). Subject to certain exceptions, personal information cannot be used without the consent of the protected principal for purposes beyond the scope of the disclosed purposes of use (Article 16). The purposes of use can be modified by the information handler only to an extent that can reasonably be considered relevant to the original purposes (Article 15). Personal information organized into a database constitutes personal data and the information handler cannot, in principle, disclose personal data to third parties without the consent of the protected principal (Article 23).

Disclosure during Due Diligence

While there is an exception to the provision requiring the information handler to seek the consent of the protected principal in order to disclose personal data to third parties in the event of a succession of business such as a merger, this exception unfortunately does not extend beyond the actual succession and is not likely to be available for the due diligence phase of a contemplated merger or acquisition. This presents a problem because entities intending to acquire the business of another entity will often need to have access to the personal data regarding the employees in the target entity during the due diligence phase.

It is in many cases effectively impossible to seek the consent of the employees in the target entity to the disclosure of their personal data during or even after the due diligence phase of a contemplated merger or acquisition. Accordingly, the parties may have to narrow the scope of employee information subject to the due diligence process so that it does not constitute personal data. This could make it difficult for the acquirer to estimate the value of, or risks associated with, the target entity.

PIPA Compliance Issues

Further to the difficulties surrounding disclosure of personal data during the due diligence process is the possibility that the target business is in violation of the PIPA. Given that the penalties for violating the PIPA include subjecting the violating entity to administrative and criminal sanctions, and the possibility of civil liability to protected principals for privacy infringements, it is critical that the acquirer be capable of assessing the target's compliance with the PIPA prior to acquisition. This may be difficult in practice however, and the acquirer may wish to obtain appropriate representations and warranties; coupled with corresponding indemnity commitments from the target business or its controlling entity.

In addition, it is worth noting that the use of personal information acquired through succession will still be subject to the original purpose of use as disclosed to the protected principal. This could potentially limit the value of the personal information to the acquirer.

Conclusion

As the PIPA potentially applies to all private entities conducting business in Japan, and the consequences for breaching the PIPA can result in administrative and criminal sanctions as well as civil liability, particular attention must be paid to compliance with the Act when considering any merger or acquisition in which personal information is involved.