

Amendments to the FIEA - Exemption from the TOB regulations (“5% exceed rule”) relating to PTS

As of October 31, 2012, the amendments (“Amendments”) to the Order for the Enforcement of the Financial Instruments and Exchange Act and the relevant Cabinet Office Ordinance in relation to the exemption from the takeover-bid (“TOB”) regulations relating to Proprietary Trading Systems (“PTSs”) have become effective. This news letter outlines the Amendments in so far as they relate to the exemption from the TOB regulations applicable to PTSs.

1. Background

(1) The TOB regulations

In summary, under Japanese law, where a purchase of shares or certain equity-related securities of a listed company is made outside a stock market or an “organized over-the-counter market”¹ in Japan, the purchase must be made in compliance with the TOB regulations stipulated in the Financial Instruments and Exchange Act (the “FIEA”) and related subordinate regulations.

The main legislative purposes of the TOB regulations in Japan are (i) to provide general shareholders with necessary information in advance in cases where a transaction which may have an impact on the control over a listed company is made, and (ii) to provide general shareholders with an equal opportunity to consider whether or not to accept a purchaser’s offer.

(2) PTSs

Before the amendments to the Securities and Exchange Act (its name was amended to the FIEA) and related acts and regulations in December 1998 (the so-called the “Big Bang” liberalization of the financial sector in Japan), all listed shares were required to be traded only on stock markets. After the 1998 amendments took effect, (a) listed shares were permitted to be traded not only on stock markets but also outside stock markets, and (b) securities companies were permitted to operate PTSs as one of their securities businesses.

Following the financial “Big Bang” in Japan in 1998 and the first day on which PTSs were permitted to be operated by securities companies in June, 2000, the environment surrounding the use of PTSs has improved². It was believed, however, that the TOB

¹ Currently, however, there exists no such “organized over-the-counter market” in Japan.

² For example, the FSA established and published a guideline concerning the establishment of PTSs in 2000 so that the methods of the determination of trade prices using PTSs would be expanded and the rules ensuring fair trade in connection with the use of PTSs would be improved. After this, an obligation concerning the best execution policy for securities companies was introduced in 2005.

regulations were still impeding the purchase of shares through PTSs by institutional investors. Specifically, the “5% exceed rule”³, one of the TOB regulations which has been seen as impeding the purchase of shares by institutional investors, applies to purchases of listed shares through PTSs. This is because PTSs do not fall under the category of a “stock market” or an “organized over-the-counter market” under the FIEA. As a result, where an investor intends to purchase listed shares through a PTS, such investor is required to confirm its share holding ratio in the target company following the purchase and record the purchase of such listed shares within 60 days of the purchase.

2. Outline of the Amendments

(1) Amendments relating to PTSs

The Amendments intend to treat a purchase of listed securities through a PTS as an exemption from the TOB regulations in the context of the “5% exceed rule” that apply to purchases made on a stock market or an “organized over-the-counter market”. As a result of the Amendments which have taken effect, the TOB regulations in the context of the “5% exceed rule” do not apply to purchases of listed securities through a PTS where such PTS has been designated by the Commissioner of Financial Services Agency (the “FSA”) as one which meets certain criteria, which are in summary⁴:

- (a) disclosure - certain designated matters including the type and name of securities, price of securities and amount of securities which were traded shall be disclosed immediately after the trade;
- (b) trading method - the price of securities shall be determined by way of auction or order matching; and
- (c) equal opportunity for all investors - an opportunity to dispose of the securities in a timely manner shall be ensured.

Please note that even after the Amendments, the TOB regulations still apply to a purchase of listed securities through a PTS where the total shareholding ratio of the purchaser and its affiliated parties in the target company following the purchase exceed one-third (1/3)⁵.

Lastly, the Japan Securities Clearing Corporation commenced its financial instruments obligation assumption business concerning the trading of securities through PTSs as of July, 2010.

³ The “5% exceed rule” requires a purchaser to comply with the TOB procedures where the total shareholding ratio of the purchaser and its affiliated parties in the target company following the off-market purchase exceeds 5% (except where the shares are purchased from not more than 10 persons within 60 days, where persons shall include the number of counterparties to the contemplated purchase).

⁴ As PTSs which meet the requirements, SBI Japannext Co., Ltd. and Chi-X Japan Limited have been designated by the Commissioner of the FSA.

⁵ As the relevant rules are complex and a TOB requires the examination of various issues under the FIEA, the Companies Act and the rules of the relevant stock exchange on a case by case basis, further legal advice should be sought in connection with each transaction.

(2) Amendment relating to Large Shareholding Reports

In addition to the above-mentioned amendments, the relevant cabinet office ordinance concerning large shareholding reports has also been amended. In certain situations, large shareholding reports are required to include the names of counterparties and other information regarding the transactions made within the past 60 days with respect to such securities. Following the amendments, it has been clarified that the submitter may omit the names of the counterparties if the past transactions have been made through a PTS and the submitter cannot know the names of the counterparties.

3. PTSs

Recently, the total volume of shares traded using PTSs has been increasing because of the improvement in the environment surrounding the use of PTSs mentioned above. It is noteworthy that, according to statistical data published by the PTS Information Network, the total traded volume of listed shares via PTSs in 2011 was approximately 12.8 trillion yen, which exceeded that of the Osaka Securities Exchange during the same year (9.7 trillion yen).

We believe that the abovementioned amendments will also encourage trading of listed shares through PTSs. Where an investor, especially an institutional investor, intends to purchase listed securities through a PTS, it will usually prefer a PTS which meets the above criteria so that it is able to avoid the “5% exceed rule”. We therefore believe that it is important for the existing PTSs and PTSs which are to be established in Japan in the future to be aware of the above criteria.

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