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Resurgence Of M&A Activities In Japan And How Deal Levels May Be Boosted By Recent Amendments To The Companies Act *By Shigeki Tatsuno & Seiya Kai*

Recent statistics show that the number of M&A activities in Japan is bouncing back to pre-financial crisis levels. This article outlines recent M&A trends in Japan and the impact that the recent amendments to the Japan's Companies Act of 2006 ("Companies Act") may have on such trends.

Recent M&A Trends in Japan

Recent Trends

The collapse of Lehman Brothers, which tapered the availability of investment financing, ushered in a period of subdued M&A activities in Japan. This downward trend in M&A activities was, however, reversed in 2012, concurrently with the introduction of "Abenomics" in Japan.

The expansionary monetary policy underlying Abenomics, which depreciated the Japanese Yen (thereby increasing the profits of Japanese exporting companies), coupled with in-

creased M&A activities by foreign investors such as private equity ("PE") funds, has brought about general market optimism. These, in turn, have led to increased Japanese M&A activities since 2012.

There was a reported 2,285 M&A transactions in 2014 involving at least one Japanese party, which is 11.6% higher than the number of transactions reported in 2013. Of the 2,285 transactions, 1,558 involved purely domestic parties (up 11.3% from 2013), 557 were outbound M&A transactions (up 11.6% from 2013) and 170 were inbound M&A transactions (up 14.1% from 2013).

M&A activities by PE funds

There were 90 reported M&A transactions in the first quarter of 2015 involving PE funds, representing a quarter on quarter increase of 20%. This is also the highest number of M&A transactions recorded in the first quarter since 2007.

There were 360 reported M&A transactions involving PE funds in 2014, which represent a year on year increase of 54.5%. Of these transactions, 297 were between domestic parties and 63 involved the acquisition of Japanese companies by foreign PE funds.

Compared to the period before the collapse of Lehman Brothers, while "mega deals" (in terms of transaction value) are not often seen in recent M&A transactions involving PE funds, M&A transactions now typically involve mid-sized companies and transaction values of several billion yen each.

One of the features of M&A transactions involving PE funds (such as KKR's acquisition of PDJ Holdings Co., Ltd. and Bain Capital's acquisition of Macromill Inc.) is that such transactions are friendlier. This is because target companies often seek to leverage on the wide network, management expertise and substantial financial resources of PE funds to propel their growth. Many mid-sized companies which lack appropriate succession planning but are reluctant

to be acquired by rival companies also see their acquisition by PE funds as opportunities for restructuring. This accords with the perspective of many PE funds which view many financially healthy mid-sized Japanese companies with unique know-how (in the areas of, among many others, precision manufacturing, biotechnology and IT) as having growth potential, but lacking in resources to fulfil such potential. Indeed, many mid-sized Japanese companies operating from suburban areas are commonly believed to have the ability, if given adequate financial backing, to compete with bigger companies or even industry leaders.

Increase in outbound M&A activities

As stated above, there were 557 outbound M&A transactions in 2014. This represents an increase of 11.6% from 2013, and clearly indicates increasing aggressiveness on the part of Japanese companies. The rise in outbound M&A transactions may also be attributable to an increasing number of Japanese companies seeking opportunities to cooperate with PE funds, such as Macromill



Inc.'s acquisition of MetrixLab B.V. (a Dutch internet research company), with the backing of Bain Capital.

Recent amendments to the Companies Act

Overview

The recent amendments to the Companies Act, which came into effect on 1 May 2015 (the "Amendments"), have been the most major since the enactment of the Companies Act. The Amendments include significant changes to raise corporate governance standards in Japan and to regulate the relationship between subsidiaries and parent companies. These changes, in particular the introduction of a new squeeze out procedure (which is discussed in further detail below), are expected to affect certain aspects of M&A practice in Japan going forward.

The new squeeze out procedure

Before the promulgation of the Amendments, squeeze outs in Japan

had to be conducted through a complex and time consuming process which involved, among other things, the issuance of new shares by the acquirer and the passing of a special resolution approving the squeeze out by the shareholders of the target company ("Target").

The Amendments introduced a new method by which squeeze outs may be conducted in Japan. Specifically, a shareholder holding, directly or through a wholly-owned subsidiary, 90% or more of the Target's voting rights ("Special Controlling Shareholder") now has the right to request all other shareholders of the Target (including holders of share acquisition rights) to sell their shares or (as the case may be) stock acquisition rights (*kabushiki tou uriwatashi seikyu*), as long as the board of directors of the Target passes a resolution approving the Special Controlling Shareholder's acquisition of minority shares in the Target. The Special Controlling Shareholder is required, for purposes of procuring such board approval, to issue a prior no-

tice to the Target indicating its intention to acquire all minority interests in the Target ("Acquisition Notice"). The Target will be required, if and once it passes a board resolution approving the Special Controlling Shareholder's acquisition of minority shares, to either inform all minority shareholders (including holders of share acquisition rights) and registered pledgees of shares in the Target of the Acquisition Notice, or issue a public notice of the Acquisition Notice, no later than 20 days before the effective date of the intended acquisition.

The new squeeze out procedure offers a simpler and time- and cost-effective alternative to majority shareholders who wish to carry out a squeeze out. It also obviates the need for the Target to pass a special shareholders' resolution approving the squeeze out. The new squeeze out procedure is expected to simplify takeovers and acquisitions in Japan, and encourage more M&A activities in the foreseeable future.

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