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Japan: Law & Practice
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JAPAN

Law and Practice

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1. LEGAL SYSTEM

1.1 Legal System

In general, Japan is a civil law jurisdiction. Most of Japan's modern legal systems are based on continental European civil systems; however, the end of World War II also saw the introduction of some Anglo-American legal influences.

Under the Constitution of Japan, judicial power is held by the courts, which are expressly guaranteed as being independent from other branches of the government. The Japanese court system can be broadly categorised into three levels.

- At the first tier, District Courts are the main court of first instance for most cases (please note that Summary Courts may act as the court of first instance for small civil claims and minor criminal offences). This tier also broadly includes Family Courts, which hear family and juvenile delinquency matters. District Courts also act as the first level of appeal for certain Summary Court matters.
- At the second tier are the High Courts, of which there are eight. The High Court acts as the general appellate court for District Court cases, as well as certain Summary Court matters.
- At the third tier is the Supreme Court, which will generally only hear appeals on cases that involve specific questions of law.

Cases are generally determined by professional judges. However, in certain serious criminal cases (eg, offences that carry a capital sentence), there is a limited use of a jury of laypersons at the court of first instance. As a civil law system, there is no principle of binding judicial precedent. That being said, decisions of the Supreme Court are considered to be strongly persuasive and are usually taken into consideration where appropriate.

2. RESTRICTIONS TO FOREIGN INVESTMENTS

2.1 Approval of Foreign Investments

There is no general requirement for approval of all forms of foreign investment. That said, the following kinds of foreign investments, as well as certain actions against invested companies by investors, will require prior notification to the authorities (ie, the minister of finance and the competent minister). In terms of foreign investments, investors will generally have to wait for 30 days while the authorities examine the investment, which includes the following:

- investments from countries with which Japan does not have existing treaties regarding inward direct investments, such as Iraq and North Korea; and
- foreign investments in certain industries, such as agriculture, fishery, manufacturing, infrastructure projects, telecommunications and IT-related industries.

It should be noted that several types of exemptions from the prior notification requirement – which depend on investor's categories (qualified financial institutions or not), invested industries and companies (listed or not), acquired ratio, etc – have been introduced since 2020.

During the aforementioned period of 30 days, the authorities can issue a legally binding order for the investment to be modified or suspended in particular cases as explained in **2.2 Procedure and Sanctions in the Event of Non-compliance**. Therefore, the requirement for prior notification is, in practice, a form of approval.

2.2 Procedure and Sanctions in the Event of Non-compliance

If an investor is required to provide prior notification, the notification should be made from six

months to 30 days prior to the intended commencement of the investment.

The authorities shall examine the investments from the perspective of national security and the potential effect of the investment on the domestic economy.

The authorities may recommend a modification or cancellation of the investment. As a recommendation, the investor will still have the discretion to accept or reject such a recommendation. However, should the investor reject the recommendation, the authorities can issue a legally binding order for the investment to be modified or suspended.

If an investor is required to provide prior notification but fails to do so, that investor is generally liable to a sentence of imprisonment of up to three years and/or a fine that shall be calculated based on the total value of the investment. However, if an investor is a corporation, a sentence of imprisonment is not applied. The authorities also have the power to order the investor to perform all acts necessary to undo an illegal investment, including the disposal of any capital that the investor acquired as a result of the illegal investment.

2.3 Commitments Required From Foreign Investors

There are no typical conditions. However, as previously mentioned, if an investor is required to provide prior notification, the authorities may recommend a modification or cancellation of the investment, and should the investor reject the recommendation, the authorities can issue a legally binding order for the investment to be modified or suspended.

2.4 Right to Appeal

An affected investor can challenge a decision of the authority that negatively affects or suspends the investment to the higher authorities or in the court. The challenge to the higher authorities can be made within three months of the date when the investor becomes aware of the decision of the authorities and within one year of the date when the decision of the authorities is made. The challenge in the court can be made to the District Court within six months of the date when the investor becomes aware of the decision of the authorities and within one year of the date when the decision of the authorities is made.

3. CORPORATE VEHICLES

3.1 Most Common Forms of Legal Entities

The most common types of corporate vehicles in Japan are the stock company (*kabushiki kaisha*) and the membership company (*mochibun kaisha*). A stock company is the vehicle that is typically used. In a stock company, the liability of shareholders is limited to the value of their shares and there is generally no assumption of additional liability by the shareholders to creditors of the stock company.

In order to establish a stock company, there is no specified minimum amount of share capital or a minimum number of shareholders. There is also generally no limitation on the purposes for which a stock company can be established to the extent they are commercial, and a stock company can be established for more than one purpose.

As for membership companies, there are three types in Japan:

- the general partnership company (*gomei kaisha*);
- the limited partnership company (*goshi kaisha*); and
- the limited liability company (*godo kaisha*).

The general partnership company and the limited partnership company are less commonly used, and the most common membership company is the limited liability company.

In the case of a limited liability company, the liability of the members of the company is limited in the same way as a stock company. The main difference between a limited liability company and a stock company is that in the case of a limited liability company, only members of the company can hold positions of management, whereas the management of a stock company is not exclusive to members of the company.

3.2 Incorporation Process

The main steps involved in the incorporation of a stock company are as follows:

- preparation of the articles of incorporation and the certification of the articles by a notary public;
- determination of the share issuance, share subscription and shareholders at the point of incorporation;
- determination of the appointment of key organs such as the directors and the company secretary; and
- registration of the stock company for incorporation with the relevant authorities.

On the specific step of share subscription, there are two ways this can be done when incorporating a stock company. The party(ies) incorporating the stock company can subscribe for all the shares at the time of incorporation, or it/they can only partially subscribe to the shares, with the remainder of the shares being subscribed by external investors. Share subscription that involves external investors typically involves more stringent procedures, in order to provide some degree of protection for the external investors.

3.3 Ongoing Reporting and Disclosure Obligations

A stock company must provide, for the inspection of shareholders, the annual financial statements of the stock company at its head office and branch offices at least two weeks before its annual shareholders' meeting. In addition, changes of management and amendments to certain items in articles of incorporation must be registered with the relevant authorities.

A listed stock company has more stringent disclosure obligations, namely:

- financial statements must be disclosed on a quarterly basis; and
- material corporate information such as a change of the representative director and the declaration of dividends must also be disclosed from time to time.

3.4 Management Structures

While it is possible for a stock company without a board of directors to make decisions concerning the organisation, operations and management via director(s) or the shareholders' meetings, many stock companies have a board of directors who are in charge of making the day-to-day decisions of the company. Depending on the stock company, it may also have other appointments, such as company auditor(s), a board of company auditors, accounting auditor(s), accounting adviser(s) and other committees. The company's management structures shall be set out in the articles of incorporation.

A shareholders' meeting can make decisions on the operation, etc, of the company. A company must hold at least one shareholders' meeting in a year.

For companies with a board of directors, the types of decisions that can be made by a shareholders' meeting are limited to those that are

stipulated in the Companies Act and the articles of incorporation. In general, decisions relating to the management of the company shall be decided by the board of directors.

The board shall consist of at least three directors, who are to be elected at the shareholders' meeting.

Resolutions of the board shall be passed via a majority vote of the directors present at the meeting.

There shall be at least one representative director. Representative directors have the power to represent the company, such as to execute documents as a representative of the company with third parties.

The company shall be audited by the company auditor(s), the board of the company auditors, or external auditors (as the case may be), who shall also audit the directors' execution of duties.

3.5 Directors', Officers' and Shareholders' Liability

The directors of the stock company have a legal duty of care to execute their duties according to the standard of a reasonably prudent manager.

The directors also owe a duty of loyalty to the stock company and must also comply with the relevant laws and regulations when executing their duties.

If the directors neglect their duties, they may be liable to the company for the damages caused as a result of the neglect.

A director can be exempt from liability via a unanimous vote of all shareholders.

There are no articles in the Companies Act that provide that directors may be liable to the company for damages arising from the performance of the directors' functions, where such performance does not amount to a neglect of duties.

While there is some recognition of "piercing the corporate veil" in Japan, this is not founded on statutory law and only exists as a matter of judicial precedent.

4. EMPLOYMENT LAW

4.1 Nature of Applicable Regulations

There are many labour-related laws in Japan, all of which were enacted to embody the fundamental principles and rights provided in the Constitution. In particular, the Labour Standards Act (LSA) and the Labour Contract Act (LCA) provide for the fundamental principles of individual labour relationships, while the Labour Union Act (LUA) provides for the fundamental principles of collective labour management relationships.

Japan is a country with a continental law system, in which judicial precedents do not have legal binding force. However, in the field of labour and employment law, judicial precedents are considered very important because it is often difficult to make decisions based only on the laws and regulations, as the provisions thereunder are abstract.

4.2 Characteristics of Employment Contracts

Form of Employment Contract

An employment contract may be executed verbally. However, to avoid any misunderstanding regarding major employment conditions, the LSA requires an employer to prepare a document clearly describing those conditions and to deliver it to a new employee upon entering into an employment contract (LSA, Article 15). Examples of major working conditions include the term of employment, the location of the workplace,

the job description, the working hours, whether overtime work will be necessary, a description of days off, the leave policy, the wages to be paid and the grounds for termination of employment.

In addition, if an employer usually employs ten or more employees, the employer must establish the rules of employment, which consist of a set of documents stipulating the specific details of the employment conditions. In addition, a copy of the rules of employment must be submitted to the labour standards inspection office together with a written opinion regarding the rules of employment from either: (i) the labour union to which a majority of employees of the workplace concerned belong (majority labour union); or (ii) if such a union does not exist, an employee representing a majority of the employees at the workplace concerned (employee representative) (LSA, Articles 89 and 90). The contents of the rules of employment must be made available to employees at all times for inspection (LSA, Article 106).

Duration of Employment Contract

The two main types of employment contract that exist in Japan are:

- those with a fixed term; and
- those with an indefinite one.

In practice, regular employees are usually hired with an indefinite term.

Under the LSA, the maximum duration of a fixed-term employment contract is three years. However, the maximum duration of a fixed-term employment contract in relation to (i) certain specialist jobs, and (ii) employees who are 60 years of age or older, is five years (LSA, Article 14).

There is no explicit minimum duration for a fixed-term employment contract. However, the LCA provides that an employer must not set a shorter term than is necessary (LCA, Article 17, paragraph 2).

Under the LCA, a fixed-term contract employee with an aggregate employment term of over five years is allowed to convert their employment contract to an indefinite-term employment contract upon request to their employer (LCA, Article 18).

4.3 Working Time

Basic Working Time Regulations

In principle, working hours of employees may not exceed eight hours per day or 40 hours per week (LSA, Article 32). Any work exceeding eight hours per day or 40 hours per week is recognised as statutory overtime work.

A rest period of at least 45 minutes must be granted during the working hours to employees who work for more than six hours, and at least 60 minutes to employees who work for more than eight hours per day. The employer must grant all of its employees a simultaneous rest period (LSA, Article 34).

Further, employees are entitled to take at least one day of holiday per week (statutory weekly holiday) (LSA, Article 35).

Article 36 Agreement

In order to have employees perform statutory overtime work or work on a statutory weekly holiday, the employer is required to execute a labour management agreement (*saburoku kyotei*) (an Article 36 agreement) with the majority labour union or, if such a union does not exist, with the employee representative, and submit it to the labour standards inspection office prior to commencing any statutory overtime work or work on statutory weekly holidays (LSA, Articles 32 and 36). In addition, the employer must refer to the possibility of statutory overtime work and

work on statutory weekly holidays in the rules of employment in advance of requiring such overtime work.

Extra Wages

When an employee has performed statutory overtime work or work on a statutory weekly holiday, the employer must pay extra wages for that work calculated at the rate of: (i) 125% of the normal salary per working hour for statutory overtime work of up to 60 hours per month and 150% for that exceeding 60 hours per month; or (ii) 135% for work on a statutory weekly holiday (LSA, Article 37).

An employee working between 10pm and 5am is entitled to an extra payment in accordance with a late-night-work compensation ratio of at least 25% of the normal salary per working hour (LSA, Article 37).

Employees in Managerial Positions

Employees in managerial positions are entitled to receive an extra wage for late-night work, but are not entitled to receive extra wages for statutory overtime work and work on statutory holidays (LSA, Article 41). Whether an employee is in a managerial position depends on various factors, such as the actual content and nature of the work performed by the employee, the authority, responsibility and the manner in which work is performed, as well as the salary and other compensation. Please note that the scope of employees in managerial positions is quite narrowly interpreted.

4.4 Termination of Employment Contracts

Unilateral Dismissal in General

When an employer unilaterally dismisses an employee, the employer must have an "objectively legitimate and socially justifiable cause" for the dismissal (LCA, Article 16). Otherwise, the dismissal is deemed to be an abuse of right and would therefore be null and void. There is no doctrine of employment-at-will in Japan. It is generally understood that the following five reasons constitute an objectively legitimate and socially justifiable cause for a unilateral dismissal:

- inability of the employee to offer their labour to an employer, mainly because of physical or mental disability or extremely poor performance;
- infringement of the disciplinary rules in the workplace by the employee's serious misconduct;
- redundancy;
- termination due to an agreement with a labour union; or
- termination due to an employer's liquidation if an employer is a corporate entity.

In addition, the employer must give the employee at least 30 days' prior notice of the unilateral dismissal or make payment in lieu of the notice (LSA, Article 20). Except as agreed in an employment contract or the rules of employment, an employee is not entitled to any monetary compensation upon a unilateral termination of employment.

Redundancy

A unilateral dismissal due to redundancy may occur where an employer wishes to continue business operations in Japan with a reduction in the number of employees. In this case, the employer must demonstrate an objectively legitimate and socially justifiable cause for the dismissal by satisfying all of the following four factors:

- The shedding of employees is justified by a strong financial or business necessity, such that it would be extremely difficult for the employer to continue its business without implementing a reduction of employees (and

not merely the fact that the employer would be more profitable if the employees were dismissed).
- The employer has already endeavoured to take all reasonable means to avoid dismissal of employees, such as facilitating intra-company transfers (or, in some cases, associated-company transfers), offering voluntary resignation with a certain amount of severance compensation and reducing other operating costs.
- The selection of employees for termination was conducted in a fair manner and in accordance with a reasonable and objective standard established by the employer. The selection criteria must be fair and based on a rational procedure, and not based on the employee's gender, membership in a labour union, race, creed, or other discriminatory reason.
- Sincere attempts at discussion or negotiation were undertaken, either with employees or their representative (including a labour union, if applicable), but were unsuccessful.

The regulations regarding notice period and monetary compensation are the same as those applicable to unilateral dismissal in general.

4.5 Employee Representations

Employee Representative

As previously explained, when an employer establishes the rules of employment, the employer must obtain a written opinion of the majority labour union or, if such a union does not exist, of the employee representative. Similarly, if an employer intends to execute certain labour management agreements, such as an Article 36 agreement, the labour management agreement must be executed with the majority labour union or, if such a union does not exist, with the employee representative. An employee representative shall be elected by a majority vote or majority consent of the employees.

Labour Union

Under the Constitution of Japan, workers have the right to form and join unions, the right to bargain collectively through the unions to which they belong and the right to engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection (Constitution, Article 28).

A union may represent its members' interests in bargaining with its members' employers in relation to the conditions of employment and other matters relating to the treatment of union members. A union does not need authorisation from administrative agencies to represent its members in bargaining with their employer(s).

If a union requests a collective bargaining session, the employer may not reject that request without a reasonable cause (LUA, Article 7, item 2).

5. TAX LAW

5.1 Taxes Applicable to Employees/ Employers

Employees are subject to income tax and local inhabitant tax in relation to their salary, and their employers must withhold such taxes, which are payable to national and local governments.

For the purpose of Japanese income tax, an individual, including an employee, is categorised as:

- a permanent resident;
- a non-permanent resident; or
- a non-resident.

A resident is defined as any individual who has their residence (*jusho*) in Japan, or has had their temporary residence (*kyosho*) in Japan for more than one year. A permanent resident is defined as a resident other than a non-permanent resi-

dent (as defined below) and is subject to income tax with respect to all of their income (including salary, hereinafter the same in this section) that they have inside and outside Japan.

On the other hand, a non-permanent resident, who is defined as any individual who is a resident of Japan, but is not a Japanese national, and who has had residence in Japan or temporary residence in Japan for five years or fewer in total, over the past ten years, is subject to income tax only with respect to income other than foreign-sourced income and any amount of foreign-sourced income that is paid in or transmitted to Japan. A non-resident (ie, any individual other than any type of resident) is subject to income tax only with respect to domestic (Japan)-sourced income. This type of income includes salaries received for work or personal services carried out in Japan, or outside Japan by a person acting as an officer of a Japanese corporation.

For the employment earnings of a permanent resident or a non-permanent resident who has submitted a certain application and whose individual income does not exceed JPY20 million per year, such an employee will only be subject to withholding tax and need not file their own tax return. Instead, the employer will be responsible for the calculation and payment of such employees' taxes (this system, especially the year-end recalculation procedure of the system, is called the "year-end adjustment system" (*nenmatsu chousei*) of tax payment). The income tax rates are progressive and the maximum rate is 45% (excluding local income tax). Additionally, reconstruction special income tax will be imposed on income tax at a rate of 2.1% from 2013 to 2037. Please see the progressive income tax rates (including reconstruction special income tax) below:

- 5.105% (for the portion of taxable income of JPY1.95 million or less);
- 10.21% (for the portion of taxable income of more than JPY1.95 million to JPY3.3 million);
- 20.42% (for the portion of taxable income of more than JPY3.3 million to JPY6.95 million);
- 23.483% (for the portion of taxable income of more than JPY6.95 million to JPY9 million);
- 33.693% (for the portion of taxable income of more than JPY9 million to JPY18 million);
- 40.84% (for the portion of taxable income of more than JPY18 million to JPY40 million); and
- 45.945% (for the portion of taxable income of more than JPY40 million).

Employees and their employer jointly contribute in equal parts to employee social expenses, such as national health insurance premiums and employees' pension insurance premiums.

In addition, if an employee dies, their heirs would be subject to inheritance tax. In general, inheritance tax is imposed on both domestic and foreign assets. However, depending on the nationalities and residence period of the decedent and their heirs in Japan, the taxable assets may be limited to domestic ones in some situations. On or after 1 April 2021, in cases where foreign individuals who have certain types of working visas die in Japan, their heirs without Japanese nationality would be subject to inheritance tax only on domestic assets, as long as they:

- are not Japanese residents at the time of the decedent's death; or
- have lived in Japan with certain types of visas for a period not exceeding ten years in the past 15 years before the decedent's death.

5.2 Taxes Applicable to Businesses

A company doing business in Japan is subject to various taxes.

Corporate income tax must be paid where a company has its head office or principal office in Japan (such a company is a "domestic corporation"). If a company does not have its head office or principal office in Japan (such a company is a "foreign corporation"), the company must pay corporate income tax only on domestic-sourced income. As for some categories of income, such as dividends and interest, income tax shall be withheld at the time of payment, but corporations can credit the amount of such income tax from the amount of corporate income tax subject to certain limitations.

Inhabitant tax and enterprise tax must be paid if a company has its head office or principal office in Japan, or permanent establishment in Japan.

Consumption tax, which is a type of value-added tax, must be paid if a company conducts certain kinds of transactions, such as sales of goods, leases of goods and provisions of services in Japan; certain categories of digital services provided to Japan; and importation transactions. Notwithstanding the above, with some exceptions (eg, if a company's capital is JPY10 million or more), consumption tax shall be exempted if the amount of taxable sales in the base period, which is the fiscal year two years prior to the current fiscal year, is less than JPY10 million.

In addition to the above, there are other taxes, such as fixed property tax, stamp duty, registration tax and real estate acquisition tax.

5.3 Available Tax Credits/Incentives

Corporations can credit the amount of income tax withheld at source from the amount of corporate income tax imposed. Income tax withheld at source is theoretically recognised as corporate income tax that is collected in advance; therefore, such an amount can be deducted from the final tax amount.

Domestic corporations are eligible to credit the amount corresponding to corporate income taxes paid in foreign countries from the amount of corporate income tax imposed in Japan, although the amount of such credit is subject to certain limitations. The purpose here is to avoid the multiple imposition of tax in different countries on the same income. Foreign corporations that have permanent establishments in Japan are also allowed to claim foreign tax credit with regard to income, which is attributable to their permanent establishments in Japan and taxable status in Japan.

Other than the above, there are various tax exemptions or tax reductions that encourage investments and R&D in Japan. For example, companies that file a blue-form tax return are eligible to credit a certain percentage of R&D expenditure from the amount of corporate income tax.

5.4 Tax Consolidation

There are two regulatory frameworks in Japan in respect of a group taxation scheme: the full controlling interest framework and the group calculation framework. The latter was introduced in the 2020 tax reform to replace an older framework known as the consolidated return framework, and becomes effective for any business years starting on or after 1 April 2022.

The full controlling interest framework applies mandatorily to intra-group transactions (including transactions involving transfers of assets, losses, dividends and interest) where all companies in the group are wholly owned (whether directly or indirectly) by the ultimate parent of the group, regardless of whether the ultimate parent is a foreign or domestic company or individual, provided that the parties to the relevant transaction are domestic companies. Under this regulatory framework, taxation on intra-group profits from transfers of certain kinds of assets – such

as fixed assets, securities, monetary claims and deferred assets (qualifying assets) – is deferred until those assets are transferred outside the group. Additionally, intra-group contributions, donations and dividends are disregarded. If the full controlling interest framework is applied, certain tax incentives to which corporations with stated capital of JPY100 million or less are normally entitled would no longer be available to a small or medium-sized company that is fully controlled by a large corporation with a stated capital of JPY500 million or more.

On the other hand, the group calculation framework, if approved by the Commissioner of the National Tax Agency (NTA), is only applicable to groups in which all companies are wholly owned (whether directly or indirectly) by the ultimate parent of the group and the companies of the group consist only of domestic companies. Under this framework, corporate income tax is calculated on a group-wide basis (ie, offsetting profit and loss among the group corporations), but payable by each group corporation.

Regarding group corporations, unrealised profits and losses of qualifying assets will not be imputed to taxable income or losses, as long as certain requirements (which are consistent with those of tax-qualified reorganisation) are met (eg, where these subsidiaries are expected to remain directly or indirectly wholly owned). The Certain NOL (net operating loss) Limitation (Japanese Separate Return Limitation Year Rule) is also applied to group corporations.

In addition, under the group calculation framework, taxation on profits from intra-group transfers of assets is deferred until those assets are transferred outside the group. Intra-group contributions, donations and dividends are also disregarded under the group calculation framework.

5.5 Thin Capitalisation Rules and Other Limitations

Japanese tax law includes thin capitalisation rules. Under these rules, if interest is paid to a foreign controlling shareholder by a domestic corporation while the payer's average interest-bearing debt to the foreign controlling shareholder in the financial year exceeds three times the value of the foreign controlling shareholder's equity interest in the payer in the said financial year, and the payer's average aggregate interest-bearing debt in the said financial year exceeds three times the value of the aggregate equity interest in the payer, the interest income related to the excess debt will not be deductible from the payer's taxable income. A domestic corporation may, however, apply a different debt-to-equity ratio (instead of three times) if it can prove that a different ratio is appropriate in light of the debt-to-equity ratio of similar corporations.

In addition, under the earnings stripping rules, with some exceptions, when interest payments (excluding those which are included in the taxable income of a recipient under Japanese tax laws) exceed 20% of the statutory adjusted income of the payer, the portion of interest payments exceeding 20% of the statutory adjusted income of the payer is not deductible from the payer's taxable income in the financial year. The earning stripping rules are also applicable to the calculation of a foreign corporation's Japan-sourced income even if such income is not attributable to the permanent establishment of the foreign corporation in Japan or if the foreign corporation has no permanent establishment in Japan. However, such excess portion is carried forward for seven financial years and can be used as deductible expenses until the total amount of deductible expenses reaches a 20% threshold in each of the following seven financial years.

5.6 Transfer Pricing

Under Japanese transfer pricing rules, a domestic corporation that transacts with related foreign entities (such as a foreign parent corporation) will, if the transaction involves non-arm's-length consideration, be liable for tax calculated based on an arm's-length consideration imputed on the transaction. In calculating the appropriate arm's-length consideration, the tax authority will apply the most suitable statutory method of calculation available.

Typically, the tax authority will request further information from the taxpayer that will help the authority to calculate an appropriate arm's-length consideration. Where a taxpayer fails to adequately respond to such requests, or does not promptly provide such information, the tax authority will have the right to determine such arm's-length consideration as it deems fit based on reasonable assumptions applicable to the relevant statutory method of calculation.

In addition, concerning transfer price documentation, four types of documentation are required:

- a NUPE (Notification for Ultimate Parent Entity) form;
- a CbCR (country-by-country report);
- a master file; and
- a local file.

Of these, the former three types of documentations are applicable to subsidiaries or branches in Japan that are constituent entities of a specified multinational enterprise (MNE), and the local file is applicable to all corporate taxpayers engaging in transactions with foreign affiliates.

5.7 Anti-evasion Rules

Japanese tax laws contain general avoidance rules such as the disallowance of acts or calculations:

- by family-owned corporations;
- in relation to organisational restructuring;
- by corporate groups of the group calculation framework; and
- regarding foreign entity profits that are attributable to a permanent establishment.

Recently, these anti-evasion rules have been applied especially to several corporate intra-group reorganisations. Those cases have subsequently developed into tax disputes.

6. COMPETITION LAW

6.1 Merger Control Notification

Prior notification is required for share acquisitions, mergers, splits, joint share transfers and acquisitions of business or assets, etc, that meet certain criteria.

The filing thresholds are different for each of the above-mentioned types of transactions. The major transactions are as follows.

- Share acquisitions:
  - (a) the total sales in Japan of the acquiring company and other companies within the same combined business group as the acquiring company exceed JPY20 billion;
  - (b) the total sales in Japan of the acquired company and all of its subsidiaries exceed JPY5 billion; and
  - (c) the ratio of voting rights of the acquiring company upon the acquisition newly exceeds 20% or 50%.
- Mergers:
  - (a) the total sales in Japan of at least one party to the merger and other companies within the same combined business group as the party exceed JPY20 billion; and
  - (b) the total sales in Japan of at least one other party to the merger and other

companies within the same combined business group as the other party exceed JPY5 billion.

- Acquisitions of business or assets, etc:
  (a) the total sales in Japan of the acquiring company and other companies within the same combined business group as the acquiring company exceed JPY20 billion; and
  (b) the total sales in Japan attributable to the business or assets to be acquired by the acquiring company exceed JPY3 billion.

Please note that "combined business group" of a party refers to a group consisting of the ultimate parent company of the party and the subsidiaries of the ultimate parent company. No filing is required for a transaction within the same combined business group.

With respect to joint ventures, it is necessary to analyse if each step of a transaction to establish a joint venture constitutes one of the above types of transactions that would be subject to the prior notification requirement and whether the relevant filing thresholds are met.

Even if a contemplated transaction is not subject to the prior notification requirement, if the transaction would substantially restrain competition in any relevant market, the transaction would be prohibited under the Antimonopoly Act.

According to the Policies Concerning Procedures of Review of Business Combination, as amended in 2019, the Japan Fair Trade Commission (JFTC) recommends voluntary filing for transactions that do not meet the mandatory filing thresholds only because the acquired company does not satisfy the monetary thresholds, but that have an acquisition value exceeding JPY40 billion, if one or more of the following factors are met:

- the business base or R&D base of the acquired company is located in Japan;
- the acquired company conducts sales activities targeting Japanese consumers, such as providing a website or a pamphlet in Japanese; or
- the total sales in Japan of the acquired company and its subsidiaries exceed JPY100 million.

6.2 Merger Control Procedure

If a contemplated transaction is subject to the prior notification requirement, the relevant enterprises are prohibited from closing the transaction for a period of 30 calendar days after formal filing (Phase I review period). If the JFTC forms the view that the transaction does not give rise to concerns over competition, the JFTC issues a clearance within the Phase I review period. However, if the JFTC forms the view that a more detailed review is required, the review process moves into a Phase II review. At the beginning of the Phase II review, the JFTC will request for additional information and the Phase II review will continue for 120 calendar days from the formal filing or 90 calendar days from the date of the receipt of all the additional information requested, whichever is the longer period.

Parties planning to file a notification may consult the JFTC not only on the descriptions of the notification form, but also on the substantive issues such as market definition and competitive assessment at the pre-notification stage. In practice, unless the transaction is very straightforward without any potential substantive issues, it is common to go through the pre-notification consultation, and the JFTC commences its review of the market situation and the potential substantive issues at the pre-notification stage.

If it is evident that the transaction would not restrain competition in any relevant market and the notifying parties request the JFTC to short-

en the waiting period in writing, the JFTC may shorten the waiting period.

6.3 Cartels

Certain anti-competitive agreements and practices such as price fixing and bid rigging are prohibited as an unreasonable restraint of trade under the Antimonopoly Act. Unreasonable restraint of trade is defined as business activities by which any enterprise, in concert with other enterprises, mutually restricts or conducts their business activities in such a manner as to fix, maintain or increase prices, or to limit production, technology, products, facilities or counterparties, thereby causing a substantial restraint of competition in any relevant market.

As for the interpretation of the elements of unreasonable restraint of trade, it would be worth noting that although "substantial restraint of competition" is one of the elements of unreasonable restraint of trade, the JFTC can easily prove that such a requirement is satisfied in the case of extreme cartel behaviour such as price fixing and bid rigging, and thus it would be difficult to justify extreme cartel behaviour in practice.

Major methods of enforcement against unreasonable restraint of trade are cease and desist orders, and surcharge payment orders. However, criminal penalties are also available. The amendment to the surcharge payment system came into effect on 25 December 2020. The amount of surcharge is calculated by multiplying the amount of sales of the target products or services during the period in which the unreasonable restraint of trade occurred (the maximum period is ten years) by the surcharge percentage rate. The rate is 10% in principle, but it can be lower depending on the size of the alleged violators, or higher if there are aggravating factors (such as repeated violation).

A leniency system for an unreasonable restraint of trade is available in Japan. The surcharge reduction rate, which was amended on 25 December 2020, is determined in accordance with the order of application for leniency as well as the degree of co-operation by the offender with the JFTC. In addition, a Determination Procedure was introduced on 25 December 2020 to protect attorney-client communications in respect of legal advice regarding the alleged violations to which leniency is applicable ("Specified Communication"). The scope of the protection under the Determination Procedure is limited compared to that which is available in similar circumstances in the USA or EU. The requirements to qualify for protection under the Determination Procedure include:

- the fact that the contents of the Specified Communication are recorded is indicated on the document itself (eg, "Specified Communications under JFTC Investigation Rules" is written or printed on the cover);
- the documents are stored separately from other documents that are not subject to the Determination Procedure; and
- the company submits an application form for the Determination Procedure as well as a privilege log that states an outline of the relevant documents.

The recent Supreme Court decision confirmed that even if the alleged price cartel occurred outside Japan, the Antimonopoly Act can apply if said cartel impedes competition in the Japanese market.

6.4 Abuse of Dominant Position

Certain types of unilateral conduct and economic dependency are prohibited as private monopolisation and unfair trade practices under the Antimonopoly Act.

Private monopolisation is defined as any conduct to exclude or control the business activities of other enterprises, thereby causing a substantial restraint of competition in any relevant market. The methods of enforcement against private monopolisation include cease and desist orders, surcharge payment orders and criminal punishment.

Various types of conduct are designated as unfair trade practices, such as:

- refusal to trade;
- unjustly low-priced sales;
- resale price restrictions; and
- abuse of superior bargaining positions.

In connection with economic dependency regulations, abuse of superior bargaining positions is the major type of misconduct to be considered and enterprises are prohibited from imposing terms and conditions that are disadvantageous to other enterprises, by unjustly leveraging their superior position over other enterprises.

All types of unfair trade practices can be subject to cease and desist orders. However, the surcharge payment order and/or criminal penalties are applicable only to certain types of unfair trade practices.

In order for conduct to be considered as private monopolisation, it is necessary to prove that it results in a substantial restraint of competition. On the other hand, a tendency to impede competition is all that is required for conduct to fall within the scope of unfair trade practices. In other words, it can be said that a higher threshold (regarding detrimental effect) needs to be satisfied in order to show the existence of private monopolisation, in comparison to unfair trade practices.

Although extraterritorial applicability of regulations on private monopolisation and unfair trade practices is not such a prominent topic of discussion, it would appear, nevertheless, that the same approach that is taken towards unreasonable restraint of trade is likely to be taken in relation to private monopolisation and unfair trade practices.

The Commitment Procedure, which is a scheme to voluntarily resolve suspected violations via mutual consent between the JFTC and the relevant enterprise, came into effect in December 2018. Ten cases regarding private monopolisation and unfair trade practices have been resolved in the Commitment Procedure as of May 2022.

7. INTELLECTUAL PROPERTY

7.1 Patents

The Intellectual Property Basic Act of Japan recognises the importance of IP protection as well as the idea of creating a vibrant economy and society by creating new IP. In Japan, IP is mainly protected by the Patent Act, the Utility Model Act, the Trademark Act, the Design Act, the Plant Variety Protection and Seed Act, the Act on the Circuit Layout of Semiconductor Integrated Circuits, the Copyright Act and the Unfair Competition Prevention Act.

Patent rights, etc, are granted by registering with the Japan Patent Office. On the other hand, the Copyright Act protects copyrights without requiring any special formalities. Although there is no property right attached to trade secrets, the Unfair Competition Prevention Act protects trade secrets as “legally protected interests”.

Japan is a party to the Patent Cooperation Treaty, the Paris Convention for the Protection

of Industrial Property, the Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks, the Hague Agreement Concerning the International Registration of Industrial Designs, the Berne Convention, the International Convention for the Protection of New Varieties of Plants and other major IP-related treaties.

A person that invents an invention with industrial applicability is entitled to obtain a patent for that invention. "Invention" in the Patent Act is defined as a highly advanced creation of technical ideas utilising the laws of nature.

A person applying for a patent must submit a written application to the Japan Patent Office. A description, scope of claims, required drawings and a summary must be attached to the application. The legal requirements for obtaining a patent are:

- industrial applicability;
- novelty; and
- inventive step.

A patent right shall become effective upon successful registration. The duration of a patent right, in principle, expires after a period of 20 years from the filing date of the original application.

The patent holder has an exclusive right to commercially exploit the patented invention.

As for remedies for infringement, the patent holder may file a claim for an injunction; a claim for disposal of infringing compositions, etc; a claim for damages; a claim for restoration of credibility; or a claim for restitution of unjust enrichment. There are presumptive provisions regarding the amount of damages that may arise as a result of the infringement of patent rights.

Acts of importing products that infringe patent rights are subject to border control measures under the Customs Act. Any intentional infringement of a patent right is also subject to criminal penalties.

7.2 Trade Marks

An applicant may apply to register a trade mark to be used in connection with goods or services pertaining to the business of the applicant. "Trade mark" in the Trademark Act is defined as any character, figure, sign or three-dimensional shape or colour, or any combination thereof; sounds; or anything else specified by cabinet order that can be perceived by people.

A person requesting a trade mark registration must submit a written application to the Japan Patent Office. Upon filing an application, one or more goods or services for which the trade mark shall be used must be described in the written application. The legal requirements for the registration of a trade mark are:

- the trade mark is to be used in connection with the goods or services for which the trade mark is registered;
- the trade mark is capable of distinguishing itself from other goods or services; and
- the trade mark is not unregistrable for reasons of public interest.

A trade mark right shall become effective upon successful registration. The duration of a trade mark right is ten years from the date of registration, but may be renewed by the holder of the trade mark right by filing an application for registration of renewal.

The holder of a trade mark right shall have an exclusive right to use the registered trade mark in connection with the designated goods or designated services. The holder of the trade mark right may also prohibit a third party from using a

trade mark that is similar to the registered trade mark.

As for remedies for infringement, the holder of a trade mark right may file a claim for an injunction; a claim for disposal of infringing compositions, etc; a claim for damages; a claim for restoration of credibility; and a claim for restitution of unjust enrichment. There are presumptive provisions regarding the amount of damages that may arise as a result of trade mark infringement.

Acts of importing goods that infringe trade mark rights are subject to border control measures under the Customs Act. Any intentional infringement of a trade mark right is also subject to criminal penalties.

7.3 Industrial Design

A creator of a design that is industrially applicable may be entitled to obtain a design registration for that design. "Design" in the Design Act is defined as the shape, patterns or colours, or any combination thereof, of an article (including a part of an article) or a building (including a part thereof), or a graphic image on a screen (including a part thereof; but such protection of a graphic image or a part thereof is limited to those for use in the operation of a device or those displayed as a result of a device performing its functions) that creates an aesthetic impression through the eye. Building interior designs are also eligible for a design registration under the Design Act.

A person requesting a design registration must submit a written application to the Patent Office. Drawings, photographs, models or specimens must be attached to the written application. The legal requirements for obtaining a design registration are:

- industrial applicability;
- novelty; and
- the design is innovative and without precedent.

A design right shall become effective upon registration. The duration of a design right, in principle, expires 25 years from the date of the application for design registration.

The holder of a design right has the exclusive right to commercially exploit the registered design and designs similar thereto.

As for remedies for infringement, the holder of a design right may file a claim for an injunction; a claim for disposal of infringing compositions, etc; a claim for damages; a claim for restoration of credibility; or a claim for restitution of unjust enrichment. There are presumptive provisions regarding the amount of damages that may arise as a result of an infringement of design rights.

Acts of importing products that infringe design rights are subject to border control measures under the Customs Act. Any intentional infringement of a design right is also subject to criminal penalties.

7.4 Copyright

A person who creates a work (the author) enjoys the moral rights of an author and the copyright with regard to the work. "Work" in the Copyright Act is defined as a creatively produced expression in which thoughts or sentiments are expressed and that falls within the literary, academic, artistic or musical domain.

The moral rights of authors include:

- the right to make a work public;
- the right to attribution; and
- the right to integrity.

The copyright includes the right of reproduction, the right of stage performance and the right of

musical performance, the right of on-screen presentation, the right of public transmission, the right of recitation, the right of exhibition, the right of distribution, the right of transfer, the right of rental and the right of adaptation.

Certain neighbouring rights are also granted to performers, producers of phonograms, broadcasters and cable-casters organisations.

There are no formalities that have to be met in order to enjoy the legal rights under the Copyright Act.

The duration of a copyright begins at the time the work is created. A copyright subsists for a period of 70 years after the death of the author.

The copyright does not prohibit (and hence does not restrain other persons from) the reproduction of the work for private use, the exploitation of works concerning incidental subjects, work in the course of consideration and any other exceptions separately provided for in the Copyright Act. In recent years, a number of more flexible exceptions have been introduced to promote the use of artificial intelligence and big data.

If the ownership of copyright is transferred to another person, the licensee has the right to continue to use the work as a matter of course.

As for remedies for infringement, the author, the copyright holder, the holder of the right of publication, the performer or the holder of the neighbouring rights may file a claim for an injunction; a claim for disposal of infringing compositions, etc; a claim for damages; a claim for restoration of credibility; or a claim for restitution of unjust enrichment. There are presumptive provisions regarding the amount of damages that may arise as a result of an infringement of copyrights.

Acts of importing products infringing copyrights are subject to border control measures under the Customs Act.

Any intentional infringement of a copyright is also subject to criminal penalties. A copyright infringement is, in principle, a crime subject to prosecution after a complaint has been made. However, following the conclusion of the Trans-Pacific Partnership Agreement, distributing pirated copies of movies over the internet has become a crime in and of itself, and no longer requires a complaint.

7.5 Others

Devices relating to the shape or structure of an article or a combination of articles are protected by the Utility Model Act without any requirement of a substantial examination to be conducted.

Computer programs contained in software are mainly protected by the Copyright Act as copyrighted works of program. Also, software-related inventions may be granted patents, provided that they involve hardware control or process-using hardware. Designs, flowcharts and manuals contained in software are protected by the Copyright Act as copyrighted works of language or of diagrams.

No sui generis database right exists in Japan. Copyright protection extends to databases if they constitute a creation by reason of the selection or systematic construction of information contained therein.

Trade secrets are protected by the Unfair Competition Prevention Act. “Trade secret” in this Act is defined as technical or business information useful for business activities, such as manufacturing or marketing methods, that are kept secret and that are not publicly known. A trade secret infringement may give rise to a suit for an injunction, a claim for damages or a claim for

recovery of credit, etc. There are presumptive provisions regarding the amount of damages that may arise as a result of an infringement of trade secrets. In a lawsuit for the infringement of business interests by unfair competition, if a court decides that it is necessary to maintain the secrecy of trade secrets held by a party to the lawsuit, a confidentiality protective order or a suspension of disclosure (including omitting an examination of the parties) may be issued. A trade secret infringement with a high degree of illegality is also subject to criminal penalties.

New plant varieties are protected by the Plant Variety Protection and Seed Act.

The circuit layout of semiconductor integrated circuits is protected by the Act on the Circuit Layout of Semiconductor Integrated Circuits.

8. DATA PROTECTION

8.1 Applicable Regulations

The Act on the Protection of Personal Information (APPI) is the main piece of legislation governing the handling of personal information by business operators (information handlers) in Japan.

Examples of APPI regulations with which information handlers are required to comply are as follows.

Purposes of Use

An information handler must specify the purposes for which it will process personal information and must not process personal information beyond the scope of the specified purpose without first obtaining the consent of the relevant data subject (APPI, Articles 17 and 18).

An information handler must not process personal information in manners that could facilitate or lead to illegal or improper activities (APPI, Article 19).

Collection of Personal Information

An information handler must not collect personal information using fraudulent or other unjust means. In principle, an information handler must not acquire certain sensitive personal information without obtaining the data subject's prior consent (APPI, Article 20).

If personal information is collected, an information handler must promptly notify the relevant data subject of, or announce, the relevant purposes of use (APPI, Article 21).

Limitation on Transfer of Personal Data to Third Parties

In principle, an information handler must not transfer personal data to third parties, including its affiliated companies, without the prior consent of the data subject (APPI, Article 27). Further, in principle, an information handler must obtain the prior consent of the relevant data subject before providing their personal data to a third party in a foreign country and provide certain information to the relevant data subjects when obtaining their consent (APPI, Article 28).

An information handler must keep records regarding transfer and receipt of personal data (APPI, Articles 29 and 30).

Security Measures

An information handler must take reasonable steps to keep personal data as accurate and up to date as is necessary to achieve the purposes of use (APPI, Article 22). An information handler must take all necessary and proper measures to ensure that personal data is kept secure from loss and from unauthorised access, use and disclosure (APPI, Article 23). Further, an information handler must exercise necessary and appropriate supervision over its employees who handle

personal data and over its data management outsourcing entities to cause them to implement and comply with security measures (APPI, Articles 24 and 25).

Data incidents, such as leakages, loss of or damage to personal data must be reported to the Personal Information Protection Commission (PPC) and the relevant data subject must be notified thereof when the incident reaches a certain threshold (APPI, Article 26).

Data Subject's Right

Upon the request of a data subject, an information handler must inform regarding the purposes of use of their personal data, give access to it, correct or delete it, or take other appropriate measures (APPI, Articles 32 to 39).

8.2 Geographical Scope

The APPI regulates the processing of personal information by information handlers in Japan. Therefore, foreign companies doing business in Japan must comply with the APPI when they process personal information.

In principle, the APPI does not apply to the processing of personal information outside Japan. However, if a foreign company that does not have an office in Japan processes personal information of a data subject in Japan in relation to sales of goods or provision of services to individuals or entities in Japan, the foreign company is required to comply with the APPI even if personal information of that data subject is processed outside Japan (APPI, Article 166).

8.3 Role and Authority of the Data Protection Agency

The PPC is the primary authority with oversight over the APPI. The PPC is an independent administrative commission that ranks at the national administrative level similar to that of the JFTC and the National Public Safety Commission. The PPC is composed of a chairperson and eight members, as well as a secretariat.

As previously explained, in the event of data incidents, an information handler must notify the PPC of them. The PPC can request a report from an information handler or conduct an on-site inspection, if necessary, for compliance with the APPI. If an information handler breaches the provisions of the APPI, the PPC will first advise the information handler to cease or correct the violation. If this advice is not followed, the PPC will then issue a formal order to take the action requested in the earlier advice if the violation of important individual rights is imminent. An information handler who fails to comply with the formal order may be subject to (in the case of an individual) a fine of up to JPY1 million and/or a prison sentence of up to one year and (in the case of a corporation) a fine of up to JPY100 million (APPI, Articles 143 to 145, 173 and 179).

9. LOOKING FORWARD

9.1 Upcoming Legal Reforms

In May 2022, the Diet enacted the Economic Security Promotion Act, which contained special provisions on inventions affecting national security. The Act will become effective within two years from the date of the promulgation as far as the provisions on inventions affecting national security are concerned.

Under the Act, patent applications containing inventions in certain designated technology areas are referred to the Prime Minister for screening. The Prime Minister may issue a secrecy order if the application contains an invention the disclosure of which may highly probably be detrimental to national security. A secrecy order remains in effect for a period of not more than one year from its date of issuance, and may be

renewed for additional periods of not more than one year.

When a secrecy order is issued, the applicant:

- is prohibited from practising the invention without first obtaining a license from the Prime Minister;
- is prohibited from disclosing the invention; and
- must take measures to safeguard the secrecy of the invention.

In addition, a person who is aware of the secrecy order and has the knowledge of the invention in the performance of their duties, including by being disclosed of the invention by the applicant, is subject to the prohibitions from the disclosure and practice.

The Act prohibits anyone from filing a patent application in a foreign country for an invention made in Japan if it is not known to the public and if it falls within certain designated technology areas. The person may file a foreign patent application if the patent application was first filed in Japan and ten months have passed without the issuance of the secrecy order.

For an invention subject to the Act, there will be no patent application disclosure during the pendency of the review and the secrecy order. The application will remain pending and there will be no final rejection or allowance during the same period.

If an applicant practises the invention without licence, discloses the invention, or files a foreign patent application in violation of the Act, the patent application will be rejected by the Commissioner of the Patent Office. In addition, the Act imposes criminal penalties for violations of the Act.

The cabinet will issue basic guidelines as to general principles, procedures, and technology fields that are subject to the Act, and other matters pertaining to the non-disclosure of patent applications. Details will be formulated in cabinet orders and regulations.

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Anderson Mōri & Tomotsune is a full-service law firm with over 500 professionals that is best known for serving overseas companies doing business in Japan since the early 1950s. It is proud of its long tradition of serving the international business and legal communities, and its reputation as one of the largest full-service law firms in Japan. Its combined expertise enables it to deliver comprehensive advice on all legal issues that may arise in the course of a corporate transaction, including those related to M&A, finance, capital markets and restructuring/insolvency, and litigation/arbitration. Most of its lawyers are bilingual and experienced with communicating, drafting and negotiating across borders and around the globe. The firm's main office in Tokyo is supported by offices in Osaka, Nagoya, Beijing, Shanghai, Singapore, Ho Chi Minh City, Bangkok, Jakarta and Hong Kong. The article is assisted by the firm's associate, Tomomi Yoshikawa.

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