

MERGERS & ACQUISITIONS

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RECENT M&A-RELATED DEVELOPMENTS IN JAPAN

By Shigeki Tatsuno & Tono Sugita



The digital economy in Japan has grown at a dramatic rate in recent years. The growth in Japan's data economy has led to a marked rise in the number of mergers and acquisitions involving data aggregation, including acquisitions by tech giants and other established technology companies of innovative startups at generous valuations for the sake of increasing or maintaining market share. This development of the data economy in Japan is largely attributable to the ecosystem established by online platform operators. This ecosystem has, in turn, ushered in a virtuous cycle of continued innovation in the digital sphere, and the accumulation and utilisation of data has facilitated the constant development and creation of new businesses.

Competition law concerns

Perspective from competition law

While the growth of the data economy and the accompanying rise in related M&A activity in Japan has brought significant benefits to the Japanese economy, they have also given rise to competition law-related concerns. Recently, discussions among regulators and industry players have focused on the notification requirements applicable to mergers and acquisitions involving target companies that do not meet the conventional quantitative criteria of merger review and are, therefore, exempt from business combination assessments. Additionally, there are also concerns about how the impact of data on competition can be properly evaluated in mergers and acquisitions.

Enhancement of regulations

Many countries across the globe are strengthening their regulation of digital platform operators while taking care not to impede innovation in the digital economy. Europe, in particular, has been enhancing its regulation of large platform operators. Among other things, the European Commission (the "EC") has recently introduced the Digital Markets Act (the "DMA") to equip competition regulators with more tools to ensure fair practices with large digital platforms in the European Union (the "EU").

The equivalent of the DMA has yet to be established in Japan. Nevertheless, Japanese regulators are following the EC's lead in reviewing Japan's competition law requirements in the context of the digital economy, especially in its examination of business combinations.

The integration

A prominent example representing this trend is the acquisition of Fitbit Inc. ("Fitbit") by Google LLC ("Google") in January 2021 (the "Integration").

When news of the proposed Integration was released by Google in 2019, the relevant competition authorities – including those in Europe, Australia and Japan – began conducting in-depth investigations and reviews before eventually providing their approval for the Integration on the condition that certain remedies to rectify the anti-competitive effects of the Integration (the "Remedies") are put in place.

In particular, competition authorities in the EU, which focused their merger reviews on the interoperability of Fitbit's data and Google's operating systems, only approved the Integration on the condition that Fitbit accepts the Remedies specified by those authorities.

Recent developments in Japan

As noted above, Japanese regulators are following the lead of the EC in reviewing the competition law requirements of Japan in the context of the digital economy. More specifically, the Japan Fair Trade Commission (the "JFTC") is now taking a more robust approach in its examination of business combinations. For example, in its examination of the Integration, the JFTC went beyond traditional quantitative requirements and *prima facie* vertical and horizontal relationships to look substantively at the potential impact of the business combination on competition – taking into consideration the unique characteristics of the digital market.

This trend can generally be traced back to December 2020, when the JFTC published its updated "Guidelines for the Administration of the Antimonopoly

Law Concerning Examination of Business Combinations” (the “Business Combination Guidelines”), which is generally understood as the JFTC’s clarification of its rigorous stance in respect of merger reviews of business combinations in the digital sphere.

The Business Combination Guidelines expressly provide a method of market delineation that assumes the provision of services without charge, even though the usual method of market delineation focuses on the ability of consumers to switch to different service providers when their current service provider raises prices.

Additionally, the Business Combination Guidelines maintain that market delineation for multi-sided market platforms will be determined according to consumer segment, and competition analysis will be conducted based on the characteristics of the multi-sided market. Regarding competition analysis, the Business Combination Guidelines state that the JFTC will focus on factors like the direct and indirect network effects, switching costs, market multiplicity, and the influence of data accumulation, in addition to considerations of market share. This is noteworthy for its contrast to previous competition analyses, which focused solely on market share considerations.

Furthermore, it is stated in the Business Combination Guidelines that the JFTC will, in cases where they deem necessary, examine business combinations with an aggregate value of less than JPY 40 billion even if such business combinations do not meet the sales-based quantitative merger notification threshold.

Based on the above, the JFTC concluded that the Integration was subject to merger review, even though the Integration did not meet the sales-based quantitative merger notification threshold that would subject a business combination to review under Japanese competition laws.

Publication of competition-related digitalisation guidelines in Japan

To promote a more proactive and substantive approach to the examination of business combinations in Japan, on 16 June 2022, the JFTC published the “*Toward the Active Promotion of Competition Policy in Response to Digitalisation and Other Socioeconomic Changes - Coordination and Enhancement of Advocacy and Enforcement*” guidelines (the “Digitalisation Guidelines”).

By way of background, most merger reviews by the JFTC are concluded within the first stage, which involves a general review of a proposed business combination. Only when the JFTC deems that further examination is necessary to determine the effects of a proposed business combination on competition will it then initiate a second round review. However, the Digitalisation Guidelines explicitly outline that the following two actions, which are typically reserved for second-stage reviews, should be taken for first-stage reviews of proposed business combinations in the digital sphere.

Firstly, it is stated in the Digitalisation Guidelines that more extensive information disclosure may be requested and interviews with a broader range of third parties may be conducted as necessary in stage one merger reviews for business combinations in the digital industry.

The Digitalisation Guidelines also empowers the JFTC to request the submission of a broader range of internal documents in first-stage reviews of proposed business combinations relating to the digital industry. It is generally understood that this enables the JFTC to conduct more detailed assessments to understand the true purpose and motives underlying a proposed business combination, among other purposes.

Following the release of the Digitalisation Guidelines, the JFTC did in fact request more extensive information disclosure and conducted more extensive interviews in its first stage merger review of two digital industry-related business combinations in 2022.

Impact on M&A in Japan

The abovementioned evolution of competition law-related regulations in the context of the digital economy will likely extend to merger reviews of business combinations in other industries. More specifically, parties to M&A transactions that are subject to merger reviews can be expected to submit internal and other materials spanning a wider spectrum, including materials relating to initial discussions and analyses of a proposed transaction. This, in turn, is expected to result in heavier legal, logistical and administrative burdens on the parties of an M&A transaction.

Considering the time needed to gather the necessary internal and other materials and documents, the JFTC will likely request the first stage of a merger review, so transaction parties would be well-advised to make advance preparations with the assistance of experienced legal counsel. Indeed, such preparations should begin from or near the outset of a proposed transaction.

In anticipation of the wider range of third parties (including competitors) that the JFTC will interview for merger review purposes, transaction parties should also be mindful of the contents of their communications with external parties regarding any contemplated transaction.



Shigeki Tatsuno is a partner at Anderson Mori & Tomotsune and specializes in the area of mergers and acquisitions, joint ventures, and cross-border investments in every field, including life-science sector. Mr. Tatsuno has extensive experience in advising venture companies and advising on PE funds. He also provides advice to foreign and domestic clients on intellectual property issues/transactions and general corporate matters. He has served as a member of the Human Research Ethics Review Committee of Graduate

School of Pharmaceutical Sciences, Faculty of Pharmaceutical Sciences, the University of Tokyo since November 2014.



Tono Sugita is an associate at Anderson Mori & Tomotsune, who is engaged principally in the field of competition law and general corporate matters. Ms. Sugita also handles a broad range of matters including litigation matters and international arbitration matters. In the field of competition law, she is working on variety of matters, particularly in response to filings related to business combination regulations. She is qualified in Japan and has received LL.B from the University of Kyoto, and J.D. from the University of Kyoto, School of Law.

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MŌRI &
TOMOTSUNE**

For more information please contact:
shigeki.tatsuno@amt-law.com | +81-3-6775-1098
tono.sugita@amt-law.com | +81-3-6775-1657