

Amendments to the Foreign Investment Regulations in Japan will be implemented on 7 June 2020

Summary

Amendments to the foreign investment regulations under the Foreign Exchange and Foreign Trade Act (the **FEFTA**) have become effective on 8 May 2020 and will be fully implemented on 7 June 2020. The key points of the amendments are:

(a) **The filing threshold has been significantly tightened**

A foreign investor investing in a listed company which engages in any of the designated businesses¹ is required to file the pre-investment notification. The threshold will be tightened from 10% of the listed company's shares or voting rights to 1% of the shares or voting rights of the company.

(b) **Certain activities will also trigger the filing requirements**

In addition to, and separate from, the filing requirement crossing the investment threshold above, a pre-investment notification will also be required for a foreign investor to take the following actions at a general meeting of shareholders of an investee's company engaging in any of the designated businesses:

- (i) consent² to an agenda item concerning appointment of directors or statutory auditors of the investee company from the foreign investor itself or its "closely-related persons" – this applies to the foreign investors that have strategic investments, or a joint venture, in a Japanese company and have a right to send its nominee director to the Japanese company (whether listed or not);

- (ii) propose or consent to an agenda item concerning the transfer or abolishment of a designated business of the investee company;
- (iii) propose or consent to an agenda item concerning a statutory merger (whereby an investee company will be a dissolving company) or statutory demerger (whereby an investee company will be a splitting company) if the business to be transferred thereby includes any of designated businesses; or
- (iv) propose or consent to an agenda item concerning the disposal of all or parts of the shares in the investee company's subsidiaries engaging in any of the designated business.

(c) **Abundant exemptions become available**

In exchange for the tightened threshold for the filing, exemptions from a pre-investment notification have been introduced for a foreign investor who satisfies certain conditions as discussed further below.

(d) **List of companies that engage in the designated business**

The Ministry of Finance (the **MOF**) has issued a list of the listed companies, specifying whether each of the listed companies in Japan conducts a designated business or core designated business³, so that foreign investors can recognise whether an investment in each listed company will trigger the pre-investment notification obligations.

¹ "Designated businesses" means businesses in industries specified by the relevant notice of the FEFTA as industries that are related to national security, cybersecurity, infrastructure and protected industry, such as agriculture or fishery.

² According to the MOF's response to the public comments, "consent" generally means exercise of the voting right for the agenda in the general meeting of shareholders, but also includes instruction to a third party to exercise the voting rights or actions which can be regarded as an equivalent action to consent.

³ "Core designated business" means industries specified by the relevant notice of the FEFTA as industries that need to be strictly regulated from the perspective of national security among designated businesses. Examples of a core designated business are businesses in the industry of weapons, aircraft, and nuclear facilities.

1. Response required for each type of foreign investor

Even after the full implementation of the amendment, no additional notification is required with regard to investments made before 7 June 2020 unless additional shares are acquired on or after 7 June 2020. The actions that need to be taken by foreign investors for investments made on or after 7 June 2020 are outlined below.

(a) Foreign investors (other than those categorised in paragraphs (b) and (c) below)

(i) Foreign investors investing through a custodian

Foreign investors who acquire shares in the name of a custodian but retain the authority to exercise voting rights over the shares, or instruct the other to exercise the voting rights per its instruction, will also be subject to the notification obligations⁴.

(ii) Foreign investors investing through a discretionary investment contract

Foreign investors who own shares through a discretionary investment contract will be subject to the notification obligations, unless the investor delegates voting rights to a third party, e.g. to its investment manager.

(iii) Foreign investors investing through an investment fund

Foreign investors who invest in Japanese companies through an investment fund will not be subject to the notification obligation when foreign investors (including the foreign investor itself) own 50% or more of interests in the investment fund in aggregate and the general partner of the fund is also a foreign investor (in which case, the investment fund itself, rather than the respective investors participating in the fund, will be subject to the filing requirements).

(b) Foreign financial institutions

A foreign financial institution which is regulated/supervised under financial regulatory laws in Japan or any other equivalent laws in foreign jurisdictions⁵ will be fully exempt from the pre-investment notification requirements and will be subject only to post-investment reporting requirements if the foreign financial institution satisfies the exemption conditions (**Exemption Conditions**). For details of the Exemption Conditions, please see paragraph 4(a) below.

(c) Sovereign Wealth Funds and Public Pension Funds (SWFs):

SWFs that are accredited by the MOF as not presenting a threat to national security etc., and have entered into a memorandum of understanding with the MOF, will be exempt from the requirement to provide a pre-investment notification for their investments in a listed company that conducts any of the designated businesses but does not conduct any core designated business. They are also exempt from the requirement to provide a pre-investment notification for their acquisition of less than 10% of the shares or voting rights of a listed company that conducts any of the core designated businesses if the SWF satisfies both the Exemption Conditions and certain additional exemption conditions (**Additional Exemption Conditions**). Please see paragraph 4(b) below for details of the Additional Exemption Conditions.

2. Definition of foreign direct investment

Under the amendments, the scope of the regulated foreign direct investment has been expanded to cover certain foreign investors' actions, including:

- (a) acquisition of shares or voting rights;
- (b) consent to an agenda item to approve the substantive changes in the business purpose (only those related to a designated business) in the articles of incorporation of an investee company; provided, however, that in case the investee company is a listed company, it shall be applicable to only the foreign investor holding one third or more of the voting rights of the investee company;
- (c) consent to an agenda item to elect a foreign investor itself or its closely-related person as a director or statutory auditor of an investee company; provided, however, that in case the investee company is a listed company, it shall be applicable to only the foreign investor holding 1% or more of the voting rights of the investee company;
- (d) proposing of, or consent to, an agenda item to approve the following matters at a general meeting of shareholders of an investee company engaging in any of the designated business:
 - (i) transfer or abolishment of a designated business;
 - (ii) statutory merger (whereby an investee company will be a dissolving company) or statutory demerger (whereby an investee company will be a splitting company) if the investee company's business to be transferred thereby includes any of designated businesses;

⁴ According to the MOF's response to the public comments, when the foreign investor has the authority to exercise voting rights or instruct the other to exercise voting rights per its instruction and when there is an explicit or implicit agreement that the custodian cannot exercise the voting rights and other rights as a shareholder of the shares, the custodian is exempt from the filing obligations. This means that to the extent that those elements are met, the foreign investor, not the custodian that has actually acquired the relevant shares, should be subject to the filing requirements.

⁵ It is not clear under the FEFTA which foreign regulations are equivalent to Japanese financial regulations. However, according to the MOF's response to the public comments, as non-exclusive examples, the following foreign financial institutions will be exempt under this exemption: investment advisors regulated under the Investment Advisers Act of 1940 of the USA; authorised fund managers and alternative investment fund managers regulated under the FCA of the UK; business operators with a type 9 (asset management) licence under the Securities and Futures Ordinance regulated by the SFC of Hong Kong; and LFMC and RFMC licensed under the Securities and Futures Act regulated by the MAS of Singapore.

(iii) disposal of all or parts of the shares in the investee company's subsidiaries engaging in a designated business;

(iv) winding-up;

provided, however, that in case the investee company is a listed company, paragraphs (i) to (iv) above shall be applicable to only the foreign investor holding 1% or more of the voting rights of the investee company; and

(e) debt financing (loan and/or notes or other debt instruments) with a repayment period of more than one year that results in the aggregate outstanding amount of debt financings by such foreign investor (i) exceeding JPY 100 million and (ii) consisting of more than a half of the aggregate amount of debts owed by an investee company.

3. Share acquisition for which notification is required after amendments

In principle and subject to the exemptions described in paragraph 4 below, the following share acquisition will require a pre-investment notification:

(a) acquisition of 1% or more of the shares or voting rights⁶ of a listed company that conducts business in a designated industry; and

(b) acquisition of one or more shares or voting rights in a non-listed company that conducts business in a designated industry.

For acquisition of shares or voting rights in a company that does not engage any designated business sector, a post-investment report is required for an acquisition of 10% or more of the shares or voting rights for both listed and non-listed companies.

4. Types of exemption conditions (when acquiring shares in a listed company)

(a) Exemption for foreign financial institutions

A foreign financial institution (including securities firms, banks, insurance companies, asset management companies, trust companies, registered investment companies including mutual funds and exchange-traded funds, and high-frequency traders) that is regulated/supervised under financial regulatory

laws in Japan or any other equivalent laws in foreign countries will be exempt from pre-investment notification if the foreign financial institution meets the Exemption Conditions below:

(i) none of the foreign investor and its closely-related persons will be elected as a director or a statutory auditor of the investee company;

(ii) the foreign investor will not propose to the general meeting of shareholders that a business in a designated business sector be transferred or abolished; and

(iii) the foreign investor will not access non-public information related to business activities in a designated business sector⁷.

For the acquisition of 10% or more of the shares or voting rights, a post-investment report must be filed by the foreign financial institution within 45 days following the date when the threshold is reached. After crossing the 10% threshold, a filing will be necessary for each acquisition (ie the report will be required for the acquisition of even one share).

(b) Exemption for general investors

(i) Investment in designated business other than core designated business

Foreign investors that meet the Exemption Conditions (as set out in paragraph (a) above) will be exempt from the pre-investment notification obligations for their investment in a listed company that conducts a designated business other than a core designated business.

For the acquisition of 1% or more of the shares or voting rights, a post-investment report must be filed by the foreign investor within 45 days following the date of crossing the 1% and 3% filing threshold, respectively. After crossing the 10% threshold, a filing will be necessary for each acquisition (ie the report will be required for the acquisition of even one share).

(ii) Investment in core designated business

In addition, foreign investors that meet both the Exemption Conditions and the Additional Exemption Conditions will be exempt from the pre-investment notification obligation for their acquisition of less than 10% of the shares or voting rights in a listed company that conducts a core designated business. The Additional Exemption Conditions are defined as follows:

(A) the foreign investor does not participate in a committee that has important decision making authority regarding core sector business; and

⁶ The percentage needs to be calculated in accordance with the methods stipulated in the FEFTA. Not only shares held by the foreign investor but also shares held by their closely-related persons will be included in the calculation of the foreign investor's shareholding or voting right percentage. As the calculation method is different from the calculation method used for a large shareholding report under the Financial Instrument and Exchange Act (Act No. 25 of 1948), foreign investors need to calculate the percentage of shares or voting rights independently from the calculation for large shareholding reports.

⁷ "Non-public information related to business activities in a designated business sector" means information related to technology, results of research and development related to technology, production methods, parts suppliers, and other information of technologies or systems related to the designated business, which are managed in secret within the departments of the designated business of the investee company (excluding information of the work conditions, remuneration and other information related to officers etc. or information related to the financial status of the investee company).

(B) the foreign investor does not make proposals regarding core sector business to the Board of Directors or a committee that has important decision making authority where the proposal requires a response or action in writing by a deadline.

For the acquisition of 1% or more but less than 10% of the shares or voting rights, a post-investment report must be filed by the foreign investor within 45 days following the date of crossing the 1% and 3% filing threshold, respectively. If the foreign investor further intends to acquire 10% or more of shares or voting rights, the foreign investor must file a pre-investment notification and obtain a clearance from the authorities before crossing the 10% threshold. The foreign investor may acquire up to the number of shares as approved by the authorities through multiple transactions for the period of six months from the date of the pre-investment notification being filed.

(c) Foreign investors who will not be exempt

No exemption applies for the following foreign investors, and therefore they are subject to the notification obligations described in paragraph 3 above.

- (i) state-owned companies⁸ (however, as an exception, those SWFs that have been individually accredited by the MOF and have entered into an MOU with the MOF, can enjoy the exemption for general investors described in paragraph (b) above); and
- (ii) investors with a record of sanctions for violating the FEFTA.

⁸ "State-owned companies" means: any foreign government, foreign government agencies, foreign local government company etc.; companies in which a foreign government holds more than 50% of the voting rights, shares or investment rates; or companies in which a foreign government could control the investment.

5. List of listed companies

The MOF has recently issued a list of listed companies in Japan, specifying whether each of the listed companies in Japan conducts a designated business or core designated business, so that foreign investors can recognise whether an investment in each listed company will trigger the pre-investment notification obligations. The URL for the list is provided below. The MOF has explained that it will update the list periodically, but the specific timing of the updates has not yet been clarified.

https://www.mof.go.jp/international_policy/gaitame_kawase/fdi/list.xlsx

Your key contacts

If you have any questions concerning the issues raised above or would like to have a more detailed discussion, please feel free to contact your ordinary Allen & Overy contact or any of our Tokyo colleagues:



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