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Designing a New Takeover Regime for Japan: Suggestions from the European Takeover Rules

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I. DOUBTS AND PROBLEMS REGARDING TAKEOVER-DEFENSIVE MEASURES

1. Doubts over Takeover-Defensive Measures

To fight against the threat of hostile takeovers, a number of listed companies in Japan have introduced takeover-defensive measures. However, a noteworthy opinion has recently been heard from lawyers who have proposed takeover-defensive measures to their clients: takeover-defensive measures must be *temporary*. Under the current takeover regime in Japan which does not effectively prevent unfair practices in the context of a takeover bid, the management of listed companies has no choice but to maintain a set of stable shareholders as a pre-bid defense measure. This practice runs of course counter to the goal of improving management efficiency. When we think about the

future of the Japanese economy, we realize that it is unlikely that the introduction of rights plans (“poison pills”) as an anti-takeover defensive measures was a good choice.¹

Under the current Japanese tender offer regulation it is possible to acquire shares or make a coercive partial offer exclusively for the purpose of challenging the company’s management since there is basically no restriction on purchasing shares of a target company as long as the purchase is conducted through the market. This means that it is still possible to carry out a scheme to purchase a large volume of shares of a listed company in the market and then launch an unfeasible offer, thereby putting pressure on the company’s executives.²

Furthermore, due to the high hurdles set by courts against the introduction and implementation of rights plans as takeover-defensive measures, the acquirer can expect its economic damage to be financially covered even if a defensive measure is taken,³ in which case the offeror suffers only a limited risk from attempting an aggressive takeover.⁴

2. *Problems with Takeover-Defensive Measures Currently in Force*

The costs for introducing takeover-defensive measures must be a heavy burden on each company, as is the case with the costs for maintaining an independent committee.⁵ In the first place, it is doubtful that the members of the independent committee selected by the company are sufficiently *independent*. During the control–transfer phase, the requirements for *independence* of such committee members should be far more stringent than those for ordinary *independent* directors, but it is practically impossible to organize the committee with such highly independent persons. Furthermore, if the members of the

* I would like to express my special appreciation to the Takeover Panel (UK), Paul Davies (Oxford University), Harald Baum (Max Planck Institute for Comparative and International Private Law), Luc Thevenoz (Geneva University), Tatsuo Uemura (Waseda University), Hiroshi Oda (London University), Gleiss Lutz LLP (Stuttgart), Herbert Smith LLP (Paris), and the members of the Studying Group on European M&A at the Japanese Securities Research Institute (Chair: Hideki Kanda, University of Tokyo) and all concerned who we met in its research delegation (the staffs of regulatory authorities, academicians, lawyers, and M&A practitioners in the UK, Germany, and France) for giving me guidance and advice in the course of writing this article. Please note that what is stated in this report is ultimately based on my understanding and viewpoint, and any possible error must be attributed to me alone.

1 K. FUJINAWA, *Kenshō: nihon no kigyō baishū rūru - raitsu puran-gata bōeisaku no dōnyū wa tadashikatta ka* [Study on Japan’s takeover rules: Was it the right choice to introduce rights plans as takeover-defensive measures?], in: Shōji Hōmu 1818 (2007) 22.

2 *Id.*, 19.

3 In the Bull-Dog Sauce Case, about 23 trillion Yen were paid by Bull-Dog Sauce Co., Ltd, the target company, to Steel Partners, the tender offeror, as “compensation for the economic damage” arising from the launch of the takeover defense.

4 FUJINAWA, *supra* note 1, 21.

5 “Independent committee,” referred to here, may be called by other names, such as corporate value committee, third-party committee, special committee, etc.

independent committee are not outside directors, a question would arise as to whether such members have any *authority* to make decisions.⁶

Recently, it has become more popular in Japan to introduce “advance warning-type defensive measures,” which can be adopted by a resolution of the board of directors. Such defensive measures taken by an advance warning to a potential acquirer could be helpful for negotiations between the offeror and the target company. In this case, however, it is not the shareholders but the incumbent management who decide whether to accept the takeover bid. Therefore, it seems very unlikely that negotiations that are carried out with a defensive plan ready to be triggered would result in the success of a hostile takeover. As a consequence, it is very likely that such a decisive plan could be an obstacle, even in the case of a hostile takeover, which could have been “favorable” to shareholders.

In the Bull-Dog Sauce Case, the general meeting of shareholders of the company approved the proposal to issue without compensation, to all shareholders, share options subject to the discriminatory terms of exercise. The Supreme Court denied an injunction claimed by Steel Partners, the tender offeror (both the district court and the high court reached the same conclusion). However, it is questionable if, because of this court judgment, we can say that the Supreme Court permitted “invoking of a defensive plan based on a resolution of the general meeting of shareholders” in any case.

3. *Legality of Rights Plans and the Role of the Tender Offer System*

It is difficult to draw a general rule – “the company may reduce the shareholding ratio targeting only a particular shareholder if it is based on a special resolution of the general meeting of shareholders and it at least assures equality in economic benefits” – from the provisions of the Companies Act. In the United States, while making an offer on condition of the revocation of the rights plan, the general approach that the offeror chooses is to (i) file a motion with the court for the revocation of the rights plan, and to (ii) launch a proxy fight in an attempt to replace the current executives and have the new executives revoke the plan. When the offeror wins in either (i) or (ii), the rights plan will be revoked and the offeror will be able to go forward with the takeover action. In view of such a situation, if it is legally permissible at all to *invoke* a rights plan (poison pill) in the United States, this may suggest that a tender offer is not regarded as a means to be taken alone in the course of acquiring control over a stock company.⁷

6 K. EGASHIRA, *Burudokku jiken saikō-sai hanketsu ga nihon no baishū bōei-saku ni ataeru inpakuto* [Impact of the Supreme Court judgment in the Bull-Dog Case on the takeover defensive measures in Japan] (Tokyo 2008); K. EGASHIRA *et al.*, *Kabunushi ga katsu, kabunushi ni katsu: Purokishi faito to sōkai un'ei* [Win by shareholders, win over shareholders: Proxy fight and general meeting management], in: Shōji Hōmu (2008) 13.

7 W. TANAKA *et al.*, *Tekitaiteki baishū to kōporēto gabanansu: Burudokku sōsu jiken kettei o megutte* [Hostile takeover and corporate governance: Bull-Dog Sauce Case decision], in:

Also in Japan, it could be said that introducing a rights plan (including the issue of share options subject to discriminatory terms of exercise) as defense against a takeover is currently permitted due to insufficient confidence in the tender offer system. In this respect, there is an influential view that argues as follows: if such discriminatory terms of exercise are construed to be illegal, no rights plan would be permitted under the existing law of Japan, and in such case, management associations might take actions to introduce more powerful defensive measures against hostile takeovers through legislation by Diet members; this is why rights plans are construed to be legal.⁸ Assuming so, if the tender offer system is improved and an environment where the shareholder decision-making principle effectively functions is developed, there is a high likelihood that *invoking* rights plans will be regarded as extremely unfair practice against shareholders.

4. *Increasing Attention to the European-style Takeover Regulations*

Considering all these points discussed above, compared to the US-style regulations – where companies are basically allowed to introduce defensive measures (countermeasures) against takeovers and courts have the last word in settling disputes⁹ – we should pay more attention to the takeover rules in European countries.

Also, in Japan it often becomes an issue in courts whether the offeror is a “green-mailer” or an “abusive acquirer.” In addition to such a framework for judging the attribute of the offeror, it is also necessary to establish concrete rules by which an abusive acquirer can be selected and excluded automatically. Furthermore, in the phase to acquire control over a company, the acquirer must disclose the real beneficiaries who will benefit from the control transfer, not merely disclosing registered shareholders. It seems to me that there is a widespread notion in Japan that any conduct not prohibited by statutory law can be construed as legal and can therefore be done without problem. On the other hand, in the UK, where a specialized institution, the Takeover Panel, that consists of M&A specialists regulates and supervises takeovers promptly and on a consultation basis, companies basically do not introduce defensive measures. We should seriously discuss the idea of importing these rules and to abolish poison pills.

Burudokku sōsu jiken no hōteki kentō [Legal study on the Bull-Dog Sauce Case] Bessatsu Shōji Hōmu 311 (2007) 50.

8 K. EGASHIRA, *Jizen no baishū bōei-saku: Hatsudō-ji no mondai* [Takeover defensive measures introduced in advance: Problems occurring upon launch], in: Hō No Shihai 145 (2007) 28.

9 Another big problem is that it takes too much time to obtain a court’s decision. Although it is difficult to simply compare the number of days required for individual suits, in the United States – where about one-third of takeover cases are brought to courts – it is said that even the Delaware state courts, which have established a reputation for handling cases promptly, need at least several weeks on average, or even as much as several months, to reach a conclusion on a takeover dispute.

II. SUGGESTIONS FROM THE EUROPEAN TAKEOVER RULES

1. *Large Gap Between Statutory Rules and Practices*

Amid calls for reconstruction of Japan's takeover bid (TOB) rules, there has been a growing interest in TOB rules in Europe.¹⁰ I myself have done a great deal of research on the pertinent rules of various European countries, including the UK, for several years, and I strongly feel that we often misunderstand the real picture when we only look at written rules. It is very important to understand dynamic structures concerning the balance between rules and practices, including social norms.¹¹

2. *"Shareholder Decision-making" in TOB in Europe*

First, we must be aware of the fact that a consensus of "shareholder decision-making" is generally strong concerning TOB rules in Europe. We also need to understand that the meanings of "shareholder decision-making" and "maximizing shareholder values" are completely different. A TOB is a system based on "shareholder decision-making." Shareholders voice whether they accept an offer. In the US, however, with its advocacy of "maximizing shareholder values," a poison pill (rights plan) has been widely adopted and the power of management is strong. There has been a notable deviation from "shareholder decision-making" in takeovers.

It is believed that an easy adoption of defensive measures such as poison pills against the offer might cause the directors' liability. Therefore, not only in the UK where institutional investors have huge influence, but also in Germany where workers have strong power, defensive measures have rarely been taken against TOB. This is generally true in European countries.

In order to make the "shareholder decision-making" principle work, sufficient and reasonable information disclosure is ensured, including the information of substantial beneficiaries.¹² In addition, appropriate timetables are prepared and prohibition of unfair trading is strict.¹³

10 I thank Miss Miki Ihara (Waseda Institute for Corporation Law and Society) for her great help in checking this part of my English draft.

11 See: H. WATANABE, *Seitei-hō ni motozukanai kigyō baishū kisei to sono henyō: EU kigyō baishū shirei no kokunai hōsei-ka to eikoku teiku ōbā paneru* [Non-statutory takeover rules and their metamorphoses: Transportation of the EU Takeover Directive into national law and the UK Takeover Panel] (Tokyo 2009); H. KANDA (ed.), *Shijō torihiki to sofutorō* [Market transactions and soft law] (Tokyo 2009); M. BURIAN / J. ROBINSON / H. WATANABE, *Eidoku no kigyō baishū rūru no jittai to wagakuni e no shisa* [Practices of takeover rules in the UK and Germany, and their suggestions to Japan], in: *Kigyō to hō sōzō* 23 (Tokyo 2010); and H. SEGAIN / A. CHANOUX / H. WATANABE, *Furansu no kigyō baishū rūru no jittai to baishū bōei-saku* [Practices of takeover rules and defensive measures in France], in the same quarterly magazine.

12 *Disclosure of substantial beneficiaries* does not mean unlimited disclosure of investors. For instance, in UK practices, whether to disclose the names of investors depends on the types of funds – that is, those funds subject to the fund manager's discretion are required only to

3. *Distinction Between “Shareholder Decision-making” and “Worker Protection”*

It is widely known that the EU’s takeover rule stipulates the offeror’s obligation to provide information to workers of the target company as well as the workers’ rights to voice their opinions.¹⁴ However, in European countries – including the UK, Germany, and France – a consensus exists that shareholders make the final decision on the consequence of takeover bids. Also, the offer price is significant when the target company makes clear whether it recommends the offer.¹⁵ There is a distinction between “shareholder decision-making” and “worker protection” in cases of takeover.

In Germany, a surprising “balance” is maintained regarding the TOB rules. Workers’ influence is strong in Germany, which knows regulations such as the codetermination law. Adoption of defensive measures based upon approval of a general shareholder meeting or a consent of supervisory board stipulated in German takeover law seems to be very strong in rhetoric. In practice, however, defensive measures against TOB are rarely taken and the consequence of TOB is left up to the judgment of shareholders ultimately. If the offer price is high, the TOB is basically successful. Due to “potent worker protection,” however, it is difficult to run the company without workers’ cooperation even if a TOB is successful. As a result, there is little hostile takeovers, and so far the cases that started as hostile TOBs ended up as friendly ones. Germany keeps a balance by having “potent worker protection” as a “cushion (adjuster)” against “shareholder decision-making” in the case of a takeover.

In France, as well, workers are provided with opportunities under the law to take part in the TOB procedures; for example, both the offeror and the target company shall provide the relevant information for the committee of enterprise (*comité d’entreprise*), which includes representative workers of the target company as its members (Code du Travail, L2323-21). The committee of enterprise may request the offeror to state his/her opinions (Code du Travail, L2323-23), and the committee of enterprise may deprive the offeror of his voting right for the target company if the offeror fails to appear when summoned

disclose the fund names – whereas those free from the fund manager’s discretion should disclose the names of investors. The same practices are in operation in Germany.

13 For example, in the UK, there is a provision on the period during which the potential offeror should announce and publish its intention to make an offer called *put up or shut up* (Takeover Code, Rule 2.5). This provision effectively prevents the offeror from announcing a vague intention to make an offer or from withdrawing the intention, thereby confusing the management of the offeree company or manipulating stock price. Recently, France also introduced such a rule (AMF’s General Regulation, Art. 223-32 to 223-35).

14 EU Takeover Directive (Directive of the European Parliament and of the Council on Takeover Bids, 2004/25/EC (April 21, 2004)) Art. 6 (1), 8 (2), 9 (5).

15 According to the questionnaire survey conducted by the inquiry team headed for Germany (from Japan Securities Research Institute) in the summer of 2009, in the case of takeovers in that country, the validity of the offer price is the main topic in the statements made by the board of auditors of the target company.

by the committee for hearing (Code du Travail, L2323-24). Nevertheless, workers do not have the effective power to decide whether to accept or refuse the offer.

These points must be recognized as the difference from Japan's circumstances and way of thinking when we discuss takeover and workers' involvement as well as the adoption of defensive measures.

4. "Balance" and "Cushion" Regarding TOB Rules

In Europe, where "shareholder decision-making" functions well in takeovers, it is believed that adopting defensive measures such as poison pills might cause the pursuit of liabilities of the directors.¹⁶ There is little room for adopting such defensive measures. Consequently, in takeovers, will "the logic of financial capitalism" rule the world?

As mentioned above, Germany keeps a balance by having "potent worker protection" as a "cushion (adjuster)" against "shareholder decision-making" in the case of a TOB.

On the other hand, in the UK or France, a mandatory offer rule (which requires the offeror to offer all shareholders at the highest price in some previous months) is applied to the addition of shareholdings between 30% (one-third) and 50%. This plays a role as a cushion. In short, the ruling strictly restrains "acquisition of halfway control."

In the US, the adoption of poison pills also plays a role as a cushion. However, we need to note that poison pills are accompanied by the battle of proxy solicitation in the US, and that there is little possibility of considering poison pills legal in Europe.

5. "Moderate Mandatory Offer Rule" as a Basic Type in Europe

A "mandatory offer rule," adopted throughout Europe, is basically applied when more than a certain number of voting shares of a listed target company (typically 30%, or one-third of voting rights) is acquired. (This is different from Japan where "compulsory tender offer" is based on "the ratio which the offeror is about to acquire.") The basic type of this rule seems to be very strict. However, if you understand "the balance" that arises in the context of the rule, it is not so strict after all and could be "a soft cushion" as a deterrent against an easy acquisition of control.

Inhibitory effects of a mandatory bid rule on the market for corporate control and the transfer of control is often emphasized as negative side effects. But a mandatory offer

16 In the UK, where institutional investors have huge influence, most shareholders are negative about adopting defensive measures such as rights plans. Similarly, in Germany and France, the adoption of such defensive measures is generally considered to be against the *interest of enterprise* (*Unternehmensinteresse* in Germany, *intérêt social* in France) and is regarded as grounds for raising the issue of responsibility of directors, etc. However, in relation to the concept of *interest of enterprise*, there is no specific criterion as to what would or would not actually be *in the interest of enterprise* at the scene of a takeover. This concept involves the same problem as that involved in the concept of *corporate value*, which is discussed in Japan.

rule will not be an obstacle to M&A if an offer is generally made without applying the rule (voluntary offer).

In addition, the ratio of mandatory offer is generally small in transfer of control. In TOB practices in Europe, the offeror generally makes a voluntary offer by keeping his acquisitions in the market below the threshold of mandatory offer rule (the initial requirement is 30%). In voluntary offers, there is also an “obligation of whole solicitation.” It’s possible to realize “whole solicitation and partial acquisition” by determining the price strategically through a voluntary offer (and surplus selling after the buying).¹⁷ If these measures are used, the mandatory offer rule or the obligation of whole solicitation will not be an obstacle to business restructuring or hostile takeovers. The “obligation of whole solicitation” is not seen as strict among M&A practitioners in Europe.

Further, the UK rule “is ‘misunderstood’ as a typical example putting everything on TOB.” However, the reality is totally different. In most cases, British companies transfer control by allocation of new shares to third parties using “whitewash” as an “exemption of the TOB rule” (independent shareholders pass the resolution of the general meeting by applying *mutatis mutandis* only the disclosure regulation in the TOB rule). Principles and exceptions are reversed between the formal rule and the reality.¹⁸ In the UK, most TOB cases are voluntary offers.¹⁹ This does not mean that the mandatory offer rule is toothless. Because the rule itself is strict, the offeror would not easily acquire more than a 30% share in the market. We have to understand that the mandatory offer rule functions as a deterrent against easy acquisition of control in that meaning.

6. “Strict Mandatory Offer Rule” in Some Jurisdictions

On the other hand, it is necessary to consider unique social norms and the accompanying structures of shareholding in each country from other perspectives. In the UK, it is not preferable to remain a minority shareholder in a company that has block holders. It is preferable to acquire as close to 100% as possible if the ratio of shareholding is more than 30%. Therefore, there are few cases of acquiring 30% to 50% voting rights (large volume holding without acquiring control) “as a result of the offer.” The mandatory offer rule is also applied to slight additions in shareholding by more than 30% but less than 50% (Takeover Code, Rule 9.1).

Like the UK, several legal jurisdictions in Europe – such as France, Ireland, and Greece – also apply the mandatory offer rule to “30% (one-third) to 50% adding.”²⁰

17 In the US and other countries, attempts at partial acquisition of the voting rights of the target company through a takeover bid have been criticized as an abusive *two-tier bid*. In Europe, however, such attempts are effectively turned down under the regulations on the consideration to be offered when *squeezing out* minority shareholders.

18 See TAKEOVER PANEL, Annual Report.

19 *Id.*

20 France (AMF’s General Regulation, Art. 234-5); Ireland (Takeover Rules 2007, Rule 9); Greece (Takeover Law, Art. 7).

Adopting the “strict mandatory offer rule” as such will be an effective deterrent against transfer of control in the legal jurisdictions where the ratio of block holders is high. Therefore, in France and Greece, among others, it is admitted that the person who already holds the target company’s voting rights over the mandatory offer’s threshold can acquire some shares within certain consecutive months without a mandatory offer (called the “creeping acquisition rule”²¹). It is reasonable to think that such a “creeping acquisition rule” is set as a “cushion” to this type of a additional strict mandatory offer rule.

Also, in Europe as a whole, however, urgent capital infusion²² or business restructuring within a group for corporate reconstruction²³ is exempted from the application of the mandatory offer rule. It is also important to understand “the existence of legal exemption” as such.

7. *Difference Between European Countries and Japan in Terms of the Stance to Set the “Threshold”*

The *mandatory offer rule* adopted in Europe is basically applied when the offeror *has acquired* more than a certain percentage of voting rights of the target company. This is different from the regulatory rule in Japan, which is based on the percentage of voting rights that the offeror *is to acquire* “as a result of a compulsory tender offer.” Some people may think that there is, in effect, no difference between Japanese and European rules, but we regard them to be quite different. Under the European threshold rule, the offeror is not rigidly bound by the obligation of whole solicitation because it is possible to make a voluntary offer below the threshold and then adjust the offer price and the conditions of the offer, thereby strategically achieving partial acquisition.

It is said that Japan used the European rules as a model in introducing the “‘compulsory tender offer’ system.” However, the Japanese threshold set *on the basis of the percentage of shares that the purchaser intends to acquire* is an odd rule from the perspective of comparative law, and combined with additional rules recently established, such as the *speed limit*, it has become a very complicated system. In addition, it should be fully understood in Japan that the European threshold set *on the basis of the percentage of shares that the purchaser has actually acquired* can help achieve a far more flexible M&A strategy.

21 France (AMF’s General Regulation, Art. 234-5, 2% or under within 12 consecutive months); Ireland (Takeover Rules 2007, Rule 9, 0.05% or under within consecutive 12 months); Greece (Takeover Law, Art. 7, 3% or under within consecutive 12 months). A similar “creeping rule” used to exist in the UK, but now the UK (Takeover Code) doesn’t have such a rule.

22 UK: Takeover Code, Notes on dispensations from Rule 9.3 (Rescue Operations); Germany: WpÜG-Angebotsverordnung § 9 sentence 1 no.3; France: AMF’s General Regulation Art. 234-9 no. 2 etc.

23 UK: Takeover Code, Notes on Rule 9.1. 8; The chain principle, Germany: WpÜG, § 36 no. 3; France: AMF’s General Regulation, Art. 234-9 no. 7 etc.

8. *Hidden Ownership Acquired Through the Use of Equity Derivatives*

Along with the recent advances in financial innovation, equity derivatives transactions, in which voting rights are decoupled from economic interest, have often been conducted.²⁴ Ownership acquired in such transactions through the use of equity derivatives, described as *hidden ownership*, could be used to sidestep regulations such as the large-holdings report system and the TOB rules.²⁵

Since equity derivative transactions are not subject to the disclosure requirement under the large-holdings report system, the stock price of the target company does not rise to the level where it could have risen if the status of shareholding were disclosed. This makes it possible to acquire a large volume of shares without paying control premiums. Furthermore, such transactions enable the short-position holders, such as funds, to acquire a large volume of shares at a fixed price suddenly at a chosen timing, and then disclose their status, by realizing the desired position for equity derivatives under contracts. This type of transaction also facilitates funds acting in concert with each other without being observed.²⁶

The existing laws of Japan explicitly require the reporting of large shareholdings in the case of schemes offering rights to claim the delivery of shares, etc., in kind. On the other hand, a long-position holder under schemes using equity derivatives, which allow *de facto* delivery of shares, etc., in kind without contracts, can be regarded as the “person holding shares, etc., in the name of another.” However, there is no clear guideline regarding the form of the report to be made by the large shareholder under such schemes or the method of calculating the shareholding ratio that is taken into account upon making a tender offer. Under such circumstances, it remains unclear how effectively this report system works and whether compliance is secured.

Recently, the UK, Switzerland, and France have taken actions to tackle this problem by imposing general regulations on *acquisition of hidden ownership* through the use of equity derivatives, rather than stipulating a specific definition of this manner of shareholding. For Japan, the regulatory policy adopted by these European countries is a very good example of an effort to prevent the *spiral of revision and evasion of rules*. At the same time, it is important to provide appropriate exceptions so that regulations on equity

24 The generic name for Contract for Differences (CFD), Total Return Swap (TRS), Cash Settled Equity Swap, and Cash Settled Equity Option, etc., is “equity derivatives.”

25 H. WATANABE, *Ekuiti deribatibu o mochi'ita 'kakureta mochibun' no mondai: Oshū ni okeru dōkō o chūshin to shite* [Hidden ownership acquired through the use of equity derivatives: Focusing on the trends in Europe]; a report by the FINANCIAL RESEARCH AND TRAINING CENTER OF THE FINANCIAL SERVICES AGENCY (ed.), *Kin'yū kiki-go no kin'yū shihon shijō o meguru kadai* [Issues surrounding the financial and capital markets after the financial crisis] 69 *et seq.*

26 K TAKEI/ Y. OTA, *Hejjifando akutibizumu no shinchō-ryū (jō/ge)* [New tides of hedge fund activism (first and second volumes)], in: Shōji Hōmu 1840 (2008) 74 *et seq.* and 1842 (2008) 23 *et seq.*

derivatives transactions will not excessively discourage financial transactions as a whole.²⁷

The breach of the obligation to report large shareholdings and of the TOB rules constitutes a violation of the Financial Instruments and Exchange Act.²⁸ There is not yet an established theory of construing the private-law effect of such a violation of public regulations. Therefore, regulatory measures should be taken to specify the private-law effect of such a violation, e.g., *suspending the voting rights*,²⁹ which is actually enforced in European countries.

9. *Position of the Takeover Rules in the System of Law*

In the UK, the Companies Act 2006 only provides for the essential matters regarding the Takeover Panel, which is the regulatory body in charge of takeover issues, and its powers and organization. The details of the TOB rules are specified by the Takeover Code that is created and implemented by the Panel. In France, TOB rules are incorporated in different laws depending on the areas where they apply, mainly in the General Regulation of the AMF (Réglement général AMF) and the Monetary and Financial Code (Code Monétaire et Financier), and some rules are also found in the Commercial Code (Code de Commerce) and the Labor Code (Code du Travail). Other European countries, such as Germany, Belgium, Austria, and Luxemburg, have independent laws on TOB rules.

In Japan, it has been argued recently from the perspective of the *division of roles between company law* and capital market law that the issue of transfer of the control of a company should basically be regulated not by the TOB rules (under the Financial Instruments and Exchange Act) but by the Companies Act, or that the TOB rules are beyond the scope of regulations under the Financial Instruments and Exchange Act.³⁰ A contrary and influential argument is that the TOB rules are a form of regulations related to market structure, which aim to ensure that the transfer of a large volume of shares that will result in the transfer of control will be carried out not through direct dealings but in a form similar to market dealings at a competitive price, and in this

27 For instance, we can find a good example in the UK rules under which the disclosure requirement basically does not apply to equity derivatives transactions, etc., conducted by a client-serving intermediary aiming to provide liquidity to the market, FSA, Disclosure Rules and Transparency Rules (DTR) 5.3.1.

28 *Kin'yū shōhin torihiki-hō*, Law No. 25/1948, last amended by Law No. 32/2010, Engl. transl. <http://www.japaneselawtranslation.go.jp/law/detail/?ft=2&re=02&dn=1&yo=financial+instruments+exchange&x=37&y=7&ky=&page=1> (as of 2006, editor's note, last retrieved 7 October 2010).

29 Regarding the breach of the obligation to report large shareholdings, UK: Companies Act 2006, Art. 797 (1) (b); Germany: WpHG, § 28; France: Code de Commerce, L 233-14 etc.

30 For example, K. EGASHIRA, *Kaisha hōsei no shōrai tenbō* [Future prospect of corporate law] (Tokyo 2009); T. UEMURA (ed.), *Kigyō hōsei no genjō to kadai* [Current status and problems on corporate law system] (Tokyo 2009) 125.

respect, these rules should be incorporated in the Financial Instruments and Exchange Act.³¹ It should be noted, however, that even those who support the former view argue that the Companies Act should provide for a “compulsory tender offer” alone, and they do not advocate that the TOB rules should be completely moved to the Companies Act and that the disclosure rule should be repealed.³² If all of the TOB rules were moved to the Companies Act, the currently required tender offer notification or amendment thereof would no longer be submitted, and the restrictions on acts conducted in relation to a tender offer would not be applied. In the end, even the substance of the existing TOB rules would be almost lost. Therefore, due consideration should be given to the possibility that serious problems would occur in the practice of the rules.³³

Squeeze-out and sell-out, which are often carried out following a takeover bid, are restructuring procedures in general, and these matters should be provided in the Companies Act (as is common from comparative law perspective). However, this issue is different from the issue of the position of the TOB rules in the system of law.

It would be completely contrary to our intended goal if we spent more time and effort than necessary on debating the purpose of the TOB rules and the position thereof in the system of law, while paying less attention to the essential tasks, specifically the discussion of the substance of the rules and their embodiment. In the process of reconstructing the TOB rules, it would be desirable to establish them in the form of an independent law or within an independent framework of rules, following the methodology adopted by European countries.

10. *Is it True that “It is difficult for Japan, which lacks the tradition of self-regulation like ‘the City,’ to have a takeover regulatory organization”?*

With regard to the possibility of having a takeover regulatory institution in Japan, we often hear the following argument: It is difficult for Japan to introduce a takeover regulatory institution like the UK Takeover Panel because Japan does not have a tradition of self-regulation like that of the City.³⁴ This is not an appropriate view in light of the current situation of takeover regulations in the UK.

The facts are now different from the traditional understanding that the Takeover Panel is a complete self-regulatory (non-statutory) organization. We should withdraw that understanding even for the past condition. As a result of adoption of the European Takeovers Directive, the authorities and organization of the Panel are now considered to have grounds in the UK Companies Act 2006. Courts can be asked for execution.

31 T. UEMURA/N. NAKAMURA, *Taidan: Kōkai kaisha-hō to wa nani ka* [Dialogue: What is public company law?], in: *Kigyō Kaikei* 61 (2009) 61 and in: *Kigyō Kaikei* 62 (2010) 158-159.

32 EGASHIRA, *supra* note 30, 126.

33 UEMURA/NAKAMURA, *supra* note 31, 159.

34 For instance, Y. ŌTA, *Kōporēto gabanansu oyobi keiei shihai-ken sōdatsu no kisei kankei o chūshin ni* [Focusing on corporate governance and regulations on the contest for the controlling interest], in: *Kin'yū Shōji Hanrei* 1322 (2009) 14.

Despite this, the Panel still holds self-regulatory character because the Panel is authorized to make and enforce rules by law and the courts also respect the Panel's decision.

In past self-regulation, rules did not apply. Rather, it was based on the fear of a loss of reputation in the City. The system worked with strict "cold shouldering," which ensured that "the people in the City do not work for those who do not follow the Takeover rules in the City." Losing the adviser's support was fatal in the UK where both parties must have advisers from investment banks, etc. It could be said that the cold shouldering allowed enforcement against even those who were not within the City. Succeeded by the Financial Services Agency as a legal rule,³⁵ this measure functioned as "self-regulation under the shadow of statutory laws."

Moreover, making consequent comparisons is very misleading. For example, the UK has "self-regulation totally relying on moral or disciplines of market participants," while Germany has "detailed and strict regulations based on the statutory law by administration (Bafin)." In early regulation by the UK Takeover Panel, the City norm called cold shouldering played an important role, as mentioned above, because the rules were brief and lacked enforcement. After the FSA was established, the FSA rule replaced the cold shouldering rule. Recently, the Code rule was upgraded to be equivalent to German rules in terms of detailed structure when a note or practice statement is included. After adopting the EU Takeovers Directive into domestic law, there is little difference between the UK and German regulatory organizations in daily practices for TOB regulations, coupled with the fact that the TOB rule was included in the statutory law (UK Companies Act 2006). Rather, what is considered an important difference between the UK and Germany includes 1) whether they can voluntarily establish and maintain concrete rules, 2) whether private M&A practitioners constitute a majority, and 3) whether they can refer to the "principle base" when it is difficult to apply the rule (currently, yes to all questions for the UK, no for Germany).³⁶

When considering the introduction of the specialized organization for takeover regulations into Japan, it is important to ensure that the supervisory body will be given the power to implement takeover rules promptly and flexibly as well as the capability of achieving personnel recruitment and rotation through exchanges with the private sector, rather than making it exist as a self-regulating (non-statutory) body.³⁷

Needless to say, *principles* alone are not sufficient for ensuring that regulatory activities fully function, but as the prerequisite for enabling the *principles-based* regulatory system to work, it is necessary to create *rules* that are detailed to some extent. Further-

35 4.3.1 R of FSA Handbook, Market Conduct (MAR).

36 In this respect, when Japan designs its own approach, the approach taken by France – vesting the government-based regulatory organization (AMF) with the comprehensive power to make rules – can serve as a good example that falls between that of the UK and Germany.

37 For instance, in Switzerland, which has takeover rules and a specialized takeover supervisory body (*Übernahmekommission*), both similar to the UK counterparts, the financial supervisory body has the power to enforce the rules.

more, the existence of *principles* facilitates the enforcement of regulations that go beyond the bounds of written *rules*, whereas *reasonable exceptions* can be provided based on *principles*. This is a key point for operating a “regulatory system that is *ultimately based on principles* where there are no written rules.”

11. *Necessity of a Takeover Regulatory Organization that is Capable of Enforcing Prompt and Consultation-based Regulations*

For predictability of the related parties, we need to have a detailed rule concerning TOB that causes transfer of control. However, it is “difficult to write down everything in the detailed rule,” including exceptions. Considering the characteristics of M&A, it is necessary to have speedy and flexible regulations applied by specialists.³⁸

In Germany, where the government agency (BaFin) is in charge of TOB regulations under statutory law, the regulatory staff finds a problem with their limited discretion in legal construction. Those engaged in regulatory activities have the common idea that they cannot take adequate measures unless necessary legislation is put in place, in order to apply the disclosure regulations to hidden ownership acquired through the use of equity derivatives, or to have the offeror who offers an inappropriate price compensate the shareholders of the target company.³⁹

Under the existing surcharge system of Japan, even an offeror who has violated the TOB rules shall be subject to a surcharge levied automatically, without room for discretionary judgment, and the amount of the surcharge tends to be huge.⁴⁰ If consultation-based TOB regulations are made possible, there will be almost no unintentional violation of the TOB rules, and even when a dispute occurs regarding the illegality of an offeror’s action, the offeror will be able to choose a scheme or action that will not be deemed to be against the rules, by consulting with the supervisory body in advance.

38 Since the Financial Instruments and Exchange Act contains a number of provisions that are so technical and complicated that it is difficult to understand their meaning after reading them only once, it is often the case that it is possible to attempt a construction that is contrary to the legislative purpose only based on the language of the Act. This is one of the reasons for calling for consultation-based regulations, see S. ŌSAKI, *KDDI ni yoru JCOM e no shihon sankā sukūmu to TOB rīru* [Capital participation by KDDI targeting JCOM, and TOB rules], in: NRI Naigai Shihon Shijō Dōkō Memo 154 (2009) 4.

39 This is based on the questionnaire survey to the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin, Federal Financial Supervisory Authority) conducted in August 2009. In current practice, in order to have the offeror who offers an inappropriate price compensate the shareholders of the target company, BaFin finds the basis for such action in the comprehensive provision on its regulatory power (Section 4 of WpÜG).

40 In the JCOM case, the point in dispute was whether KDDI evaded the TOB rule (Art. 27-2 (1) (ii) of the Financial Instruments and Exchange Act, generally known as the *one-third ownership rule*), by attempting to acquire about 37.8% of JCOM's shares through an intermediate holding company. The Financial Services Agency could have levied a surcharge of about 90 billion Yen on KDDI.

When making rules mainly targeting M&A practitioners, it is more desirable to entrust this task to a supervisory body that consists mainly of M&A practitioners and whose organization and powers are specified by statutory law, rather than to rely on defensive measures in the form of a rights plan whose legal validity is unstable.⁴¹

Assuming that a Japanese version of the Takeover Panel should be established in Japan, what kind of body would it be? It could be established as a new division of the current supervisory body, or established as a completely new organization under joint jurisdiction of several ministries and agencies. In either case, personnel recruitment and rotation would be particularly important. In Japan, personnel exchanges between the public and private sectors have recently become popular, with talented people moving from private companies to government offices on a short-term basis and then moving back after a successful tenure. The UK Takeover Panel seems to carry out such personnel exchanges and assignments systematically.

Some people propose methods other than creating a specialized body, such as appointing lawyers who are well versed in market practices as judges (on a temporary basis) or creating a new judicial division specialized in dealing with company law cases.⁴² However, takeover regulations must be enforced promptly and flexibly by experts before disputes occur, and it would be difficult to achieve this by enhancing the judicial functions. In view of this, it should not be a choice between only one of the two options, either *enhancing the judicial functions* or *creating a specialized organization for takeover regulations*; instead, we should explore both possibilities.

12. Conclusion: Future Vision for Japan's TOB Rules

The mandatory offer system is one of the main issues in the debate about reconstructing the Japanese TOB system. However, in this Japanese debate there is confusion because opinions are divided regarding the definition of the "mandatory offer." The "mandatory offer" system in Europe consists of the following rules: (i) the offeror shall solicit all shareholders; (ii) the highest price shall be determined within a certain period before the offer; and (iii) the offeror shall be prohibited from setting the conditions of the offer. In Europe, it is a common practice that, on the assumption of the existence of the mandatory offer system under which all of the rules indicated in (i) to (iii) shall apply, less restrictive regulations are actually enforced, and voluntary offers that satisfy only (i) are generally used. This is an important point that we should keep in mind as the premise for debate.

41 As for the legal instability of rights plans, see H. WATANABE, *Nihon-ban teikuōbā paneru no kōsō* [Designing the Japanese version of a takeover panel], in: Uemura (ed.) *Kigyō hōsei no genjō to kadai* [Current status and problems of the corporate law system] (Tokyo 2009) 21–22.

42 For instance, N. MATSUO, *Baishū bōei-saku to kōkai kaitsuke kisei no arikata (kin'yū shōji no me)* [Takeover defensive measures and desirable takeover rules (Eye of financial commerce)], in: *Kin'yū Shōji Hanrei* 1299 (2008) 1.

In the course of reconstructing specific rules in Japan, we should aim to prevent coercive offers (pressure on shareholders to sell their shares against their will), and at the same time, to facilitate more flexible implementation of M&A. To this end, it is desirable to set a European-type *threshold on the basis of the percentage of shares that the purchaser has actually acquired*, while maintaining it as the basic rule to solicit all shareholders. In this context, the degree of strictness of the mandatory offer rule largely depends on whether or not the rule is applied to the offeror's attempt to increase shares of the target company beyond the threshold but below the 50% level.⁴³ If we set such an *additional* mandatory offer rule, we will be able to control the level of strictness of the rule by setting conditions for *creeping* rules.⁴⁴ In the case of corporate rehabilitation or business restructuring within a corporate group, it is desirable to establish appropriate exceptions to the mandatory offer rule like those currently in force in Japan (and in European countries).

In Europe, defensive measures against takeover attempts are rarely taken, but it is not that the adoption of defensive measures is completely prohibited. The important aspect is that European countries follow the *shareholder decision-making principle* based on the TOB rules that thoroughly guarantee protection of shareholders (investors). In Japan, it is also necessary to design a framework wherein the *shareholder decision-making principle* will function, and in this process, although the adoption of defensive measures such as rights plans may not be generally appropriate, room should be left for adopting defensive measures only *as the result of the shareholder decision-making principle*.

In referring to TOB rules in major European countries, it is important to understand the structure of "a distinction between shareholder decision-making and worker protection." Regarding concrete rules, it is also important to fully understand the difference and meanings between two mandatory offer rules stated in this article and to pay attention to rational exemption or reversals between principles and exceptions in the reality (for example, "Whitewash" in the UK).

"Shareholder decision-making" has a vital role as a precondition for the smooth functioning of TOB rules. Choosing the appropriate "cushion" is important to avoid letting only the logic of financial capitalism carry through. We should carefully work on restructuring TOB rules, looking at the structure of social norms and the impact of introduction of rules.

43 For instance, most European countries, including Germany, do not have such an *additional* mandatory offer rule.

44 The *creeping* rule adopted in France is relatively easy on the offeror, whereas those in Ireland are very strict. In the UK, where there are few block holders, takeover attempts have continued to be very active even after the *creeping* rule was abolished.

SUMMARY

The article discusses the possible implications of the European takeover rules on a prospective new takeover regime in Japan. In the first part of the article, the author identifies doubts over and problems with such measures currently in force in Japan, including the legality of rights plans, and the role of the tender offer system as such. In the second part, takeover bid rules in European countries are analyzed: There is generally a strong consensus for the concept of “shareholder decision making”, which has to be distinguished from the idea of “worker protection”. “Moderate mandatory offer rules” are adopted in most European countries, whereas “strict mandatory offer rules” are preferred in some jurisdictions, including the UK. After touching – inter alia – equity derivatives transactions and the question whether it is difficult and necessary for Japan to have a takeover regulatory organization, the author draws up a future vision for Japan’s TOB rules.

(The Editors)

ZUSAMMENFASSUNG

Der Artikel erörtert die Bedeutung, die das europäische Übernahmerecht für ein potentielles neues japanisches Regelwerk bezüglich Verteidigungsmaßnahmen gegen Übernahmen haben könnte. Im ersten Teil äußert der Autor Zweifel an Maßnahmen, die gegenwärtig in Japan Anwendung finden, darunter die Rechtmäßigkeit sog. „Giftpillen“ als Verteidigungsmittel, und auch an der Regelung öffentlicher Erwerbsangebote insgesamt. Im zweiten Teil werden die Regelungen von Übernahmeangeboten in Europa analysiert. Allgemein besteht dort große Einigkeit über das Konzept einer Entscheidungsbildung durch die Aktionäre im Kontext eines Übernahmeangebots, welches von dem des Arbeitnehmerschutzes zu trennen ist. In Europa wurden in der Regel moderate Regeln für Pflichtangebote eingeführt, wenngleich einige Übernahmeregime, wie beispielsweise der Takeover Code des Vereinigten Königreiches, strengere Regeln für Pflichtangebote vorsehen. Nachdem er unter anderem Aspekte wie Transaktionen aktienbasierter Derivate und die Frage, ob es für Japan möglich und notwendig ist, eine spezielle Aufsichts- und Regulierungsinstitution für Unternehmensübernahmen zu schaffen, diskutiert hat, entwirft der Autor ein Konzept möglicher künftiger Regeln für Übernahmeangebote in Japan.

(Die Red.)