

Japan

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LAW AND POLICY

Policies and practices

1 | What, in general terms, are your government's policies and practices regarding oversight and review of foreign investment?

With a view toward enhancing the growth potential of the Japanese economy and to reinvigorate regions around the country, the Japanese government has undertaken measures to increase inward foreign direct investment (FDI). Accordingly, in 2013, the Japanese government announced its target of increasing FDI stock to ¥35 trillion by 2020, and FDI stocks have grown steadily since to ¥39.7 trillion by the end of 2020, thereby achieving the target. In June 2021, the Japanese government adopted the 'Strategy for Promoting Foreign Direct Investment in Japan', which set a new FDI target of doubling the FDI stocks to ¥80 trillion by 2030. The new strategy also established the following three points as basic pillars:

- creation of a new digital market and building of an innovation ecosystem;
- acceleration in the development of business environments in response to global environmental changes; and
- development of an investment environment through public-private partnerships utilising regional strengths.

The Japanese government actively opened its doors to foreign investors, in principle, for more than a decade after the Foreign Exchange and Foreign Trade Act (the Forex Act) was amended in 1998.

However, this trend seems to have shifted in recent years. Since 2018 the Japanese government has been gradually tightening the foreign investment regulations, and this government policy is expected to remain unchanged in the next few years. This appears to be in line with global trends such as in the United States, where the US government has recently taken aggressive measures to prevent technology leaks to foreign countries.

The Japanese government is promoting an open policy for foreign investors while scrutinising incoming investments over possible national security concerns. In August 2019, Japan added cybersecurity to the list of sectors to be protected under the Forex Act. Further, the 7 June 2020 revisions to the Forex Act, which tighten regulations on inbound equity investments, came into full effect (the 2019 Amendment).

Separately, in July 2020, the government added pharmaceuticals and medical equipment to the list of protected sectors (see below for the particular types of businesses that the Forex Act protects) to ensure a stable domestic supply of these medical products amid the covid-19 pandemic and in the event of potential future outbreaks.

In November 2021, the two new categories pertaining to certain critical minerals including rare earths were added to the list to secure a stable supply of such minerals:

- The Japanese government added the following business sectors pertaining to 34 critical minerals –
 - metals mining (including the operation of mineral exploration vessels, and land and underwater surveys for mining);
 - manufacturing, repair and maintenance of, and of software for, devices or products used for metals mining (including mineral exploration vessels, marine equipment, excavators and drilling machines); and
 - mineral analysis services.
- Construction service businesses that improve or maintain port facilities on certain islands to facilitate the activities of mineral exploration vessels.

With respect to the Forex Act procedures, in general, foreign entities investing in Japan must submit an ex post facto report to the relevant ministries. The purpose of this requirement is to enable the government to make a statistical record of the number of ex post facto reviews and government investigations.

However, the Forex Act requires that the foreign investor submit prior notification for certain investments involving (1) particular types of businesses; and (2) particular geographic areas or countries. These are as follows:

- The business-related restrictions are imposed on, among others, investments in any business related to:
 - national security (eg, weapons, airplanes, nuclear power, space development or information and communication technology);
 - public infrastructure (eg, electricity, gas, water, telecommunications or railways);
 - public safety (eg, medicine, medical equipment, vaccine manufacturing or private security service); and
 - protected domestic industry (eg, agriculture).
- The geographic-related restrictions are imposed on, among others, investments concerning countries with which Japan has not executed an FDI treaty (eg, Iran) and certain activities involving the Iranian government, entities, individuals or groups.

If the investment falls into one of the above categories, the party who intends to make such an investment is required to submit prior notification of the intended investment to the relevant ministries. The relevant ministries will then review the filed report usually within 30 days from filing. After the review, the relevant ministries may order a suspension or amendment of the contemplated investment, if they find the investment is likely to:

- impair national security;
- impede public order;
- hamper the protection of public safety; or
- have a significant adverse effect on the management of the Japanese economy.

To date, the Japanese government has rarely exercised its authority to issue an investment suspension order under the current Forex Act. In fact, since liberalisation of FDI in 1980, there has been only one case where the ministries have actually issued a suspension order.

This first, and to date only, investment suspension order was issued in 2008. At that time, The Children's Investment Master Fund (TCI), a UK-based activist fund, intended to purchase up to a 20 per cent stake in J-Power, a Japanese electric utility owning core infrastructure including nuclear plants and power lines. The relevant ministers announced that, upon their review, including a series of interviews with TCI, the investment risked impairing J-Power's financial condition, reducing future capital expenditure or maintenance spending on fundamental infrastructures, and causing negative effects on the construction and maintenance of the Ohma nuclear fuel recycling plant. A Ministry of Finance official publicly described the Japanese government's position in this instance as exceptional given that all other foreign investments have been approved since the Forex Act was enacted in 1980.

Main laws

2 | What are the main laws that directly or indirectly regulate acquisitions and investments by foreign nationals and investors on the basis of the national interest?

The Forex Act (along with supplemental regulations) is the main law.

Further, the following other laws regulate investments by foreign nationals or set the upper limit of holding ratios by foreign nationals in specific business sectors:

- the Broadcast Act;
- the Radio Act;
- the Civil Aeronautics Act;
- the Consigned Freight Forwarding Business Act;
- the Mining Act;
- the Ships Act; and
- the Act on Nippon Telegraph and Telephone Corporations.

Scope of application

3 | Outline the scope of application of these laws, including what kinds of investments or transactions are caught. Are minority interests caught? Are there specific sectors over which the authorities have a power to oversee and prevent foreign investment or sectors that are the subject of special scrutiny?

The Forex Act is applied to foreign investments carried out by foreign investors in the following situations, among others:

- the acquisition of 1 per cent or more of shares of listed companies;
- the acquisition of shares of unlisted companies from a domestic investor;
- the transfer of shares from a non-resident individual to a foreign investor (where a non-resident acquired these shares while a resident);
- when consent is sought for any material change to corporate objects, or to other matters having a material impact on the management of the target company or companies;
- the transfer of a business from a Japanese entity;
- the establishment of a branch, factory or other business office (excluding a representative office) in Japan or substantially changing the type or business objectives of such a branch, factory or other business office, excluding those with the business objectives of:
 - banking;
 - foreign insurance;
 - gas;
 - electricity;
 - certain types of securities;

- investment management;
- foreign trust; and
- fund transfer;
- the extension of loans to Japanese corporations exceeding certain thresholds; and
- the acquisition of private placement bonds issued by a Japanese corporation exceeding certain thresholds.

The following two sections look in detail at regulation under the Forex Act in the cases of an acquisition of listed company shares and an acquisition of unlisted company shares.

Acquisition of listed company shares

A foreign investor is generally required to file a prior notification if it acquires 1 per cent or more shares in a listed company that conducts business in the protected sectors under the Forex Act (Designated Business Sectors). If required, the authorities will review the transaction to determine whether the investment is likely to threaten national security, disrupt public order or hamper the protection of public safety. There are no rules or regulations requiring special scrutiny for any particular sectors in such reviews. Designated Business Sectors include:

- manufacturing of weapons and certain related products;
- manufacturing of satellites, rockets and certain related products;
- manufacturing of nuclear plants and certain related products; and
- manufacturing of semiconductor devices.

However, as the prior notification for a listed company's share purchase (PN-SP) may impose an undue burden on a foreign investor, two exemptions (discussed below) are available if three criteria (Basic Criteria) are satisfied: (1) a foreign investor or its closely related person (eg, its board member, employee, and that of its subsidiary, etc) will not become a board member of the target company; (2) a foreign investor will not propose to the general shareholders meeting a transfer or disposition of important business activities of the target company; and (3) a foreign investor will not have access to non-public information about the target's technologies that may impact Japanese national security or public welfare.

The first exemption, Blanket Exemption, is available to financial institutions that are licensed or registered under financial regulatory laws in Japan and other jurisdictions, including: securities firms; banks; insurance companies; asset management companies; trust companies (excluding those solely engaged in custody businesses); registered investment companies (including mutual funds and exchange-traded funds); and high-frequency traders (only those registered in Japan). This exemption, however, is not available to foreign state-owned enterprises (SOEs).

The Blanket Exemption provides a comprehensive exemption from filing a PN-SP. A post-facto report, however, will be required when the investor's total shareholding reaches 10 per cent or more for each transaction.

The second exemption, Regular Exemption, is generally applicable for foreign investors as well as sovereign wealth funds and public pension funds accredited by the Ministry of Finance, but not for (1) an investor with a record of sanctions for violation of the Forex Act; and (2) SOEs. The Regular Exemption's scope depends on whether a target conducts business in 'Core Sectors', which are those sectors in the Designated Business Sector that the government designates as significantly posing a national security risk (eg, armaments, aerospace, nuclear power and dual-use technologies that can be diverted to military use). Core Sectors also include oil, railways, utilities, telecommunications and cybersecurity.

If a target does not conduct business in any of the Core Sectors, a foreign investor will be exempted from filing a PN-SP. However, the

foreign investor will be required to file a post-facto report for a listed company's share purchase when the investor's total shareholding reaches: (1) 1 per cent for the first time; (2) 3 per cent for the first time; and (3) 10 per cent or more for each transaction. A post-facto report will not be required for a second and subsequent transaction reaching 1 per cent or 3 per cent.

If a target conducts business in any of the Core Sectors, a foreign investor will be exempted from filing a PN-SP only if it holds less than 10 per cent of the shares and two other requirements are satisfied: (1) the foreign investor will not attend and will not have their designated persons attend the target's board or committee meetings that make important decisions for its business in the Core Sector; and (2) the foreign investor will not make proposals in writing to the board or board members individually requiring responses or actions within a specific deadline.

Acquisition of unlisted company shares

If a foreign investor acquires one or more shares in an unlisted company that is engaged in the Designated Business Sectors from a resident of Japan, prior notification is generally required. An exemption, however, is available if the Basic Criteria are satisfied and a target does not conduct business in any of the Core Sectors. A post-facto report, however, will be required even if this exemption applies to the share purchase.

Separately, if a foreign investor acquires 10 per cent or more shares in an unlisted company that is not engaged in the Designated Business Sectors from a resident of Japan, a post-facto report is required.

Moreover, prior notification is generally required if a foreign investor acquires one or more shares in an unlisted company that is engaged in any of the Designated Business Sectors from a non-resident of Japan. A foreign investor may be able to obtain an exemption, however, if the Basic Criteria are satisfied and a target does not conduct business in any of the Core Sectors. Even with the exemption, a post-facto report will be required on acquisition of one or more shares in an unlisted company.

While prior notification is not required for a share purchase in an unlisted company that is not engaged in any of the Designated Business Sectors from a non-resident of Japan, other post-facto reports may be required depending on the method of payment that a seller and purchaser use.

Definitions

4 | How is a foreign investor or foreign investment defined in the applicable law?

The Forex Act defines a 'foreign investor' as: (1) a non-resident individual; (2) a corporation, partnership, association or other entity established under a foreign jurisdiction or having its principal office in a foreign country; (3) a corporation established under Japanese law of which the ratio of the sum of the voting rights directly or indirectly held by those listed in item (1) or (2) is 50 per cent or more, including through entities of which the ratio of the voting rights held by those listed in item (1) or (2) is 50 per cent or more; and (4) a corporation, partnership, association or other entity in which the majority of either the officers (eg, directors) or the representative officers are non-resident individuals.

Further, the definition of foreign investor for certain types of limited partnership has been changed since the 2019 Amendment. Both general partners and limited partners of a partnership had been individually subject to the notification requirement, but under the 2019 Amendment, only the partnership itself (through its general partner) will be subject to the notification requirement.

Special rules for SOEs and SWFs

5 | Are there special rules for investments made by foreign state-owned enterprises (SOEs) and sovereign wealth funds (SWFs)? How is an SOE or SWF defined?

SOEs are not able to enjoy exemptions from prior notification.

However, SWFs that are deemed not to pose a risk of threatening national security are eligible for an exemption from prior notification of a listed company stock purchase if accredited by the Ministry of Finance.

For an SWF to obtain accreditation, the Ministry of Finance will enter a memorandum of understanding (MOU) with the SWF if the Ministry believes both of the following conditions are satisfied:

- the SWF's investment activity is only for economic return; and
- the SWF's investment decision is made independently of its government.

The decisions to enter an MOU and for accreditation are not made public.

Relevant authorities

6 | Which officials or bodies are the competent authorities to review mergers or acquisitions on national interest grounds?

The Minister of Finance and the minister with jurisdiction over the targeted business are the competent authorities to review mergers or acquisitions under the Forex Act. Though the decision-making authorities are such ministers, all of the applications, notifications or post-facto reports, which are required under the Forex Act, must be submitted through the Bank of Japan.

Examples of the jurisdictions of the ministers are follows:

- the Prime Minister: banks, trusts, security business, insurance businesses and investment advisers;
- the Minister of Finance: import and export of precious metals and import and export of alcohol;
- the Minister of Agriculture, Forestry and Fisheries: agriculture and fishery and the manufacture of food or beverages;
- the Minister of Health, Labour and Welfare: pharmaceutical matters and medical devices; and
- the Minister of Economy, Industry and Technology: manufacture, sales, import and export of aircraft, weapons and electricity.

7 | Notwithstanding the above-mentioned laws and policies, how much discretion do the authorities have to approve or reject transactions on national interest grounds?

For those transactions only requiring ex post facto reports, the authorities do not have any discretion to either approve or reject the transactions as the ex post facto reports are required mostly for the purpose of statistical analysis.

However, in reviewing the transactions subject to the prior notification requirement, the authorities (the Minister of Finance and the minister with jurisdiction over the targeted business) have, theoretically, relatively broad discretion under the Forex Act.

PROCEDURE

Jurisdictional thresholds

8 | What jurisdictional thresholds trigger a review or application of the law? Is filing mandatory?

The Foreign Exchange and Foreign Trade Act (the Forex Act) imposes prior notification requirements on investments into certain limited areas of businesses and investments involving certain geographical regions.

As long as the intended investment falls into one of these categories, the filing is mandatory and there are no numerical threshold-based exemptions such as turnovers or asset size. Even in cases where the business triggering the prior notification is small relative to the size of the overall business, the filing requirement could be triggered. For instance, if an electric manufacturer's batteries are used in satellites, then prior notification might be required. As the waiting period for prior notification could delay the entire transaction, a careful review of the targeted company is highly recommended, especially when it conducts a wide range of business activities such as electronics manufacturers.

National interest clearance

9 | What is the procedure for obtaining national interest clearance of transactions and other investments? Are there any filing fees? Is filing mandatory?

The prior notification application must be submitted to the Minister of Finance and the minister with jurisdiction over the targeted businesses via the Bank of Japan. Application forms are available at the Bank of Japan's website. There are no filing fees.

The relevant ministers will review the applications, and may require hearings, written responses to inquiries and submission of additional documents.

If the investment does not fall into the categories requiring a mandatory filing, the authorities do not have power to intervene in the transaction.

10 | Which party is responsible for securing approval?

A foreign investor is responsible for securing government approval. Therefore, if the investment falls into the category triggering the need for prior notification, in Japanese business practice it is strongly recommended to include a conditions precedent clause to the consummation of the transaction so that the parties are not obliged to make the investment during the waiting period.

Review process

11 | How long does the review process take? What factors determine the timelines for clearance? Are there any exemptions, or any expedited or 'fast-track' options?

Under the Forex Act, if prior notification is required, the investor must wait to close the investment for 30 days after the Bank of Japan's acceptance of the application. However, such a waiting period normally will be shortened to two weeks from the acceptance in accordance with the relevant ordinance. Moreover, with an aim to facilitate more inward foreign direct investment, the Ministry of Finance and other relevant ministries have implemented expedited fast-track options for greenfield investment (ie, certain investments involving a wholly owned Japanese subsidiary), rollover investments (ie, certain investments, the same type of which were previously filed within six months by the same investor) and passive investments (ie, certain investments that the investor undertook so as not to proactively participate in the management or to take control of the company). If the fast-track option applies, the waiting period will be further reduced to five business days.

However, if the authority finds that there needs to be a review procedure on whether the investment is likely to threaten national security, disrupt public order or compromise public safety, the waiting period can be extended up to five months. Given the recent trend to encourage foreign investment, the Ministry of Finance and other relevant ministries may give the foreign investor an opportunity for prior consultation or may request *sua sponte* more details about the potential investment before the prior notification is submitted. Therefore, a foreign investor should be mindful that the timeline for submission of a prior notification

may be extended, especially if the foreign investor seeks to invest in one of the secured categories of business.

12 | Must the review be completed before the parties can close the transaction? What are the penalties or other consequences if the parties implement the transaction before clearance is obtained?

An investor may not close the transaction for which prior notification is required for the relevant waiting period. If the investor closes the transaction in violation of this time restriction, the investor will be subject to criminal penalties, including imprisonment of up to three years or a fine, or both. The fine will be up to three times the amount of the investment or ¥1 million, whichever is higher.

Involvement of authorities

13 | Can formal or informal guidance from the authorities be obtained prior to a filing being made? Do the authorities expect pre-filing dialogue or meetings?

The Bank of Japan accepts general enquiries about Forex Act filing procedures via the telephone.

The Ministry of Finance and other relevant ministries are generally open to pre-filing consultation for any substantive enquiries. Although such a pre-filing consultation is voluntary, it is recommended for an investor to conduct pre-filing consultations, especially if there is any ambiguity in terms of the application of relevant laws and regulations. The Ministry of Finance and other relevant ministries may also *sua sponte* request a pre-filing consultation.

14 | When are government relations, public affairs, lobbying or other specialists made use of to support the review of a transaction by the authorities? Are there any other lawful informal procedures to facilitate or expedite clearance?

The Ministry of Finance and the minister with jurisdiction over the targeted businesses will review the application. As there has only ever been one case where a suspension order was issued, investors typically do not utilise government relations, public affairs lobbyists or other specialists to support the review of the transaction. Other than cooperating fully with the review process, such as providing necessary information that is requested or promptly providing answers to enquiries, there are no other informal procedures to facilitate or expedite clearance.

The waiting period will be expedited as a default rule set by the relevant ordinance.

15 | What post-closing or retroactive powers do the authorities have to review, challenge or unwind a transaction that was not otherwise subject to pre-merger review?

The competent authorities have the power to issue an order requiring the foreign investor who failed to make prior notification to divest all or a part of the shares that were acquired or to take such other measures, if necessary, upon seeking an opinion from the Ministry of Finance's Council on Customs, Tariffs, Foreign Exchange and other Transactions.

SUBSTANTIVE ASSESSMENT

Substantive test

- 16 | What is the substantive test for clearance and on whom is the onus for showing the transaction does or does not satisfy the test?

The authorities will review an investment subject to prior notification to assess whether it is likely to threaten national security, disrupt public order, compromise public safety or have a significant adverse effect on management of the Japanese economy. For example, the Ministry of Finance and the Ministry of Economy, Trade and Information issued an order to suspend the Children's Investment Master Fund's proposed investment in a Japanese power company as there was a likelihood that the investment might compromise public safety.

The investor has the burden of proof to show that the transaction does not fall into any of the above-mentioned categories.

- 17 | To what extent will the authorities consult or cooperate with officials in other countries during the substantive assessment?

The Japanese authorities have continually stressed that the Foreign Exchange and Foreign Trade Act (the Forex Act) restrictions are consistent with international standard rules such as the Organisation for Economic Co-operation and Development Codes of Liberalisation of Capital Movements and of Current Invisible Operations. The 7 June 2020 revision to the Forex Act authorises the Japanese government to exchange information with foreign governments for the purpose of regulatory enforcement by foreign governments or authorities.

Other relevant parties

- 18 | What other parties may become involved in the review process? What rights and standing do complainants have?

Before issuing an order to suspend or change the content of an investment, the relevant ministers are required to receive input from the Ministry of Finance's Council on Customs, Tariffs, Foreign Exchange and other Transactions (the Council). The Council comprises academic experts nominated by the Minister of Finance. There are no procedures for allowing the foreign investor applicant/complainant to participate in the review process. Therefore, the complainants have no rights or standing. Moreover, competitors or customers may not be involved in the review process.

Prohibition and objections to transaction

- 19 | What powers do the authorities have to prohibit or otherwise interfere with a transaction?

The Minister of Finance and the minister with jurisdiction over the targeted business have the power to order an investor to suspend or change the content of the investment, but only upon the investor's refusal to implement the recommendation from the relevant ministers.

- 20 | Is it possible to remedy or avoid the authorities' objections to a transaction, for example, by giving undertakings or agreeing to other mitigation arrangements?

Other than regular advocacy activities, there is no remedy or way to avoid the authorities' recommendations or objections to an investment subject to the Forex Act. However, the authorities' decision can be formally challenged.

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Challenge and appeal

- 21 | Can a negative decision be challenged or appealed?

A negative decision can be appealed. A foreign investor can file an appeal with the relevant ministry challenging an order to suspend or change the content of an investment. The ministry receiving the appeal is required to hold a public hearing after giving reasonable advance notice.

A party that is dissatisfied with the relevant ministry's decision in the appeal procedure may then bring an action in court.

Confidential information

- 22 | What safeguards are in place to protect confidential information from being disseminated and what are the consequences if confidentiality is breached?

Under the National Public Service Act, government officials owe a duty of confidentiality for any confidential information of which the officials become aware in the course of their duties. As such, any confidential information provided to government officials in the foreign investment review process will be subject to that obligation. If an official were to breach his or her confidentiality obligation, he or she could incur a criminal penalty of imprisonment for up to one year or a fine of up to ¥500,000. The aggrieved party may make a claim for damages against the Japanese government, as a result of the dissemination of confidential information, if the required elements under the State Redress Act, for example, an intentional act or an act owing to the negligence of an official, can be established.

RECENT CASES

Relevant recent case law

- 23 | Discuss in detail up to three recent cases that reflect how the foregoing laws and policies were applied and the outcome, including, where possible, examples of rejections.

Since the enactment of the Foreign Exchange and Foreign Trade Act in 1980, there has been only one instance where the order to suspend the investment was actually issued (the order issued to suspend the Children's Investment Master Fund's proposed investment in J-Power in 2008), despite the fact that hundreds of prior notification applications have been filed each year.

UPDATE AND TRENDS

Key developments of the past year

24 | Are there any developments, emerging trends or hot topics in foreign investment review regulation in your jurisdiction? Are there any current proposed changes in the law or policy that will have an impact on foreign investment and national interest review?

In 2020 and 2021, the government added the following new categories of business to the list of Designated Business Sectors and Core Sectors, which requires prior notification from foreign investors.

- 2020: manufacturing businesses involving pharmaceuticals for specific infectious diseases (including pharmaceutical intermediates manufacturing businesses);
- 2020: manufacturing businesses involving specifically controlled medical devices (including accessories and parts thereof);
- 2021: business sectors pertaining to 34 critical minerals, including rare-earth metals –
 - metals mining (including the operation of mineral exploration vessels, and land and underwater surveys for mining);
 - manufacturing, repair and maintenance of, and of software for, devices or products used for metals mining (including mineral exploration vessels, marine equipment, excavators and drilling machines); and
 - mineral analysis services.
- 2021: construction service businesses that improve or maintain port facilities on certain islands to facilitate the activities of mineral exploration vessels.

Moreover, Japan's new prime minister, who was elected in October 2021, has emphasised strengthening Japan's economic security. Since there has been ongoing discussion within the government to amend the Foreign Exchange and Foreign Trade Act (Forex Act), foreign investors in Japan are recommended to seek up-to-date advice from a Forex Act expert, especially when the investor is considering investing in a Japanese company that is engaged in any of the protected sectors (ie, Designated Business Sectors or Core Sectors).