

Companies Act Reform: Organisation Restructuring/M&A (Share Purchase Demand, Injunction against Organisation Restructuring and Corporate Split)

This Briefing explains the amendment to the Companies Act and other related laws, which was enacted on 20 June 2014, focusing on:

- (i) share purchase demands, which are demands by shareholders that the company purchase their shares, in relation to business transfers and organisation restructuring (collectively, "Organisation Restructuring");
- (ii) requests for injunctions against Organisation Restructuring; and
- (iii) corporate splits.

The reform extensively amends the provisions of the current share purchase demand system with the aim of preventing the abusive exercise of share purchase demands. Moreover, the reform entrenches requests for injunctions against Organisation Restructurings in statute and sets out provisions to protect creditors from fraudulent company splits. The reform is expected to come into force by 1 April 2015.

Share Purchase Demands in relation to Organisation Restructuring

The reform has extensively amended the legal effect and procedures of the current share purchase demand system with the aim of preventing the abusive exercise of share purchase demands.

Reinforcement of Restriction on Withdrawal of Share Purchase Demands

Under the current legislation, shareholders dissenting the Organisation Restructuring may, in principle, not withdraw their share purchase demands. This is to prevent the abusive exercise of share purchase demands. However, there was no provision restricting the sale of shares which are subject to a share purchase demand ("**Subject Shares**") to third parties. Consequently, dissenting shareholders have been able to achieve the same result as withdrawing their share purchase demands through selling their Subject Shares to third parties.

Under the new legislation, the issuing company needs to create a purchase account. The dissenting shareholders are then obliged to file an application to transfer their Subject Shares to the purchase account upon exercising the share purchase demand so that they are not able to later sell the Subject Shares to third parties.

Effective Date of Purchase of Subject Shares

Under the current legislation, the effective date of the purchase of the Subject Shares is either the effective date of the Organisation Restructuring or the date on which the purchase price of the Subject Shares is paid, depending on the situation. However, it has been widely criticised that dissenting shareholders are provided with a double economic benefit where the dissenting shareholders are able to maintain their position as shareholders until the purchase price is paid, because they are entitled not only to receive dividends for the Subject Shares but also to receive statutory interest of 6% starting 60 days after the effective date of the Organisation Restructuring until the purchase price is paid.

Under the new legislation, the effective date of the purchase of the Subject Shares will be the sole effective date of the Organisation Restructuring. Consequently, the issue regarding the double economic benefit will be resolved as dissenting shareholders will lose their position as shareholders on the effective date of the Organisation Restructuring.

Payment for Subject Shares Prior to Decision regarding Price

Under the current legislation, as mentioned above, the dissenting shareholders are entitled to receive statutory interest of 6% starting 60 days after the effective date of the Organisation Restructuring until the purchase price is paid. Critics have indicated that providing such a high interest rate to the dissenting shareholders fosters the abusive exercise of share purchase demands.

Under the new legislation, a company is entitled to pay an amount it considers the fair price for the Subject Shares until the court determines a different purchase price, if it does so at all. It is expected that the number of abusive share purchase demands will be reduced by this amendment.

Share Purchase Demands in relation to Short Form Mergers and Simplified Mergers

Under the current legislation, share purchase demands may be exercised in the case of short form mergers or simplified mergers. However, it has been argued that there is no need to permit shareholders to exercise share purchase demands in the case of these mergers as they do not have a significant effect on shareholders.

Under the new legislation, shareholders cannot exercise share purchase demands for short form mergers and simplified mergers.

Practical Implications

Attention should be paid to complying with the new procedure set out to reinforce the restriction on the withdrawal of share purchase demands. Failure to comply with the procedure could cause the invalidity of the Organisation Restructuring. After the reform comes into force, transaction timetables will need to take the new procedure into account for Organisation Restructurings.

Injunctions against Organisation Restructuring in Statute

Under the current legislation, there is no provision for an injunction against Organisation Restructuring except against short form mergers.

Under the new legislation, it is expressly stated that if there is a threat to shareholders' interests and also a breach of the law or the articles of incorporation, then the shareholders are entitled to seek an injunction against the Organisation Restructuring. This reform will apply to Organisation Restructuring for which agreements and plans are entered into after the new legislation comes into force. Accordingly, if it is expected that Organisation Restructuring will be conducted after the new legislation comes into force, transaction timetables should be prepared taking into account the possibility of an injunction.

Protection of Creditors in relation to Corporate Splits

Under the current legislation, creditors who are left with the split company as a result of the corporate split ("**Residual Creditors**") do not enjoy strong protection. Consequently, provisions to protect creditors are set out under the new legislation.

Protection of Creditors against Fraudulent Corporate Splits

There were no provisions in the Companies Act which protected creditors from fraudulent corporate splits, where important business and assets were to be transferred to the successor company and creditors stayed with the split company. The Japanese courts permitted requests for the avoidance of fraudulent acts (*sagai kouji torikeshi ken*) under the Civil Code regarding corporate splits and that was the only way to claim against a fraudulent corporate split. Under the new legislation, however, creditors are permitted to directly collect their debts from the successor company extra judicially. Residual Creditors are capable of making reimbursement claims against the successor company for the extent of the value of the assets passed on to the successor company subject to the condition that the split company knew that the corporate split concerned would harm the creditors.

Protection of Creditors Unknown to Split Company

The new legislation also aims to protect creditors unknown to the split company by increasing the number of situations where they can collect debts from both the split company and the successor company.

Where Japanese legal concepts have been expressed in the English language, the concepts concerned may not be identical to the concepts described by the equivalent English terminology as they may be interpreted under the laws of other jurisdictions.

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