NORTON ROSE FULBRIGHT

Global Rules on Foreign Direct Investment

Japan

Foreign direct investments (FDI) in Japan are regulated by the Foreign Exchange and Foreign Trade Act (the FEFTA). Over the past few years, there have been major amendments to the FEFTA, with the most recent amendments coming into effect on May 10, 2022.

Under the FEFTA, a foreign investor is required to make, through the Bank of Japan, a prior notification of its FDI to the Minister of Finance of Japan and the ministers having jurisdiction over the businesses conducted by the target, if the target is in a business sector designated as sensitive to national security, public order, public safety or the smooth management of Japan's economy (Sensitive Businesses).

Expanded scope of foreign direct investments

The FEFTA amendments expanded the scope of "FDI". FDI refers to:

1 Acquisitions:

- (a) The acquisition of shares of an unlisted company (no threshold) from a domestic investor.
- (b) The acquisition of 1 percent or more of the shares or voting rights of listed companies by a foreign investor and its closely related persons (the threshold was lowered from 10 percent to 1 percent in the amendment which took effect in May 2020); or
- (c) The acquisition of business from a resident corporation.

2 Exercise of voting rights:

- (a) The acceptance of a proxy to exercise voting rights on behalf of a shareholder; or
- (b) An agreement between foreign investors jointly to exercise voting rights in a listed company, which, in either of item (d) or (e), results in a foreign investor and its closely related persons having authority to exercise 10 percent or more of the voting rights.

3 Others:

- (a) At a shareholders' meeting, approving:
- (b) A significant change in the purpose of the target's business, unless the target is a listed company and the foreign investor and its closely related persons together hold less than a third of the voting rights;
  - (i) A transfer of business in any designated business sector; or
  - (ii) The appointment of a foreign investor or its closely related person as a director or statutory auditor of the target, unless the target is a listed company and the foreign investor and its closely related persons together hold less than 1% of the voting rights in case of (f)(ii) and (iii); and
- (c) Other similar activities.

For an acquisition of shares in an unlisted company from a domestic investor, there is no threshold for the notification requirement, and even acquiring one share will trigger the notification obligation. Acquiring shares in an unlisted company from another foreign investor will not be considered as FDI for purposes of the notification requirement under the FEFTA and is called “special acquisition”. In cases of special acquisition, unless the target is conducting one of the listed businesses, the scope of which is quite limited compared to the scope of Sensitive Businesses, prior notification is not required.

Foreign investor

A foreign investor for the purposes of the FEFTA includes (a) a non-resident, (b) a corporation and other organizations established under foreign law, and (c)(i) a domestic corporation 50 percent or more of the voting rights of which are owned by a non-resident or a foreign corporation or organization, or (ii) its subsidiaries.

Restricted business sectors

Amendments which took effect in May 2020 expanded the scope of Sensitive Businesses triggering a notification obligation by adding 20 business sectors. The additional business sectors include software-related business, including contract development of software, built-in software and packaged software, and Internet use support services, which could be interpreted as including many software or Internet services. The expansion of covered business sections has a significant influence in practice. In addition, the manufacturing of medical products and devices for infectious diseases was added starting July 15, 2020 in light of the COVID-19 pandemic.

Exemptions

To strike a balance, certain exemptions from the notification requirement were introduced by the recent FEFTA amendments. Requirements for such exemption include the obligation (a) to not cause their closely related persons to become a director or statutory auditor of the target, (b) to not propose to the shareholders’ meeting a transfer of business in any designated business sector, and (c) to not access any non-public technology information of the target relating to any designated business sector. For example, a foreign financial institution is exempted from prior notification when it satisfies the above conditions (a) to (c), even if it acquires 10 percent or more of the shares or voting rights of a listed company that is engaged in a designated business. However, such exemption is not applicable to foreign governments or foreign state-owned enterprises, unless such enterprises are accredited by the Minister of Finance as not posing a national security risk.

Review process

There is a statutory waiting period of 30 days from the date of acceptance of the notification by the Bank of Japan, although such waiting period will be normally shortened to two weeks. However, it may be extended to up to five months if the authority identifies any national security concern.

The typical and recommended practice is to contact the relevant ministries in advance of the formal filing with the support of experienced lawyers and provide them with the required information such as the foreign investor’s capital structure, purpose of the investment, and plans for managing the target.

Post-closing notification

Even if the target is not engaged in any Sensitive Business, a foreign investor is required to make a post-closing notification of FDI. A foreign investor must make a notification within 45 days from the date of the investment. In addition, in certain cases, such post-closing notification is necessary even if exemptions from prior notification are applicable. There are also some exceptions to a post-closing notification requirement. For example, acquiring less than 10 percent of the shares in an unlisted company will not trigger a post-closing notification requirement.

Crypto assets

To close loopholes in economic sanctions implemented against Russia, certain capital transactions via crypto assets including the sale and purchase of crypto assets between a resident and a non-resident became subject to the FEFTA under the latest amendments to the law which took

effect in May 2022. Also, pursuant to the amendments, crypto asset exchange service providers are obligated to (a) confirm whether transactions consisting of making or receiving payments via crypto assets are subject to the economic sanctions, (b) conduct KYC processes of customers relating to such transactions and capital transactions, and (c) report to the government regarding the intermediation, brokerage or agency of capital transactions via crypto assets in excess of JPY 30 million.

By *Norihito Sato and Satoshi Tatsugawa* of Mori Hamada & Matsumoto in collaboration with Norton Rose Fulbright.

Norihito Sato

Mori Hamada & Matsumoto

Satoshi Tatsugawa

Mori Hamada & Matsumoto