Private M&A

Contributing editors
Will Pearce and John Bick

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Davis Polk & Wardwell LLP

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Preface

Private M&A 2019

Second edition

Getting the Deal Through is delighted to publish the second edition of *Private M&A*, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Brazil, Costa Rica, Ecuador, Egypt, Indonesia, Malaysia, Myanmar, Philippines, Singapore and Taiwan.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Will Pearce and John Bick of Davis Polk & Wardwell, for their continued assistance with this volume.

London
September 2018

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Japan

Kayo Takigawa and Yushi Hegawa
Nagashima Ohno & Tsunematsu

Structure and process, legal regulation and consents

1 How are acquisitions and disposals of privately owned companies, businesses or assets structured in your jurisdiction? What might a typical transaction process involve and how long does it usually take?

Acquisitions and disposals of privately owned companies are often structured through a share acquisition, which is a straightforward sale and purchase of shares of a target company through a transaction between a seller and a buyer. In addition, a share exchange is a structure that may be used to acquire shares of a privately owned company, especially when there are multiple shareholders. A share exchange is a transaction between two companies whereby one company becomes the 100 per cent shareholder of the other company. Under the share exchange, shares of the acquired company are exchanged for the shares of the acquiring company, cash or any other assets.

Acquisitions and disposals of businesses or assets are conducted through a business acquisition or a corporate split. A business acquisition is a straightforward sale and purchase of the business of a company through a transaction between a seller and a buyer. A corporate split is a transaction whereby a company splits off a segment of its business. The split-off business can be transferred to a company to be newly formed as a result of a corporate split (incorporation-type split) or to an existing company (absorption-type split). In a corporate split, shares of the company to which the split business is transferred, cash or other assets are distributed to the transferring company that splits off the business.

There is nothing unique in the transaction process in Japan, which is typically as follows:

- the parties enter into a confidentiality agreement;
- the buyer conducts a due diligence investigation over the target company, or the business or assets to be transferred;
- the parties sometimes enter in to a non-binding or binding memorandum of understanding (MOU); and
- the parties negotiate and enter into a definitive agreement.

The time necessary for the processes of acquisition to be closed and completed varies depending on factors such as scale, complexity, or structure; however, it usually takes three to six months for a share transfer to be completed, and if the structure used is a share exchange, business transfer or corporate split, the process usually takes an additional one to two months to be completed.

2 Which laws regulate private acquisitions and disposals in your jurisdiction? Must the acquisition of shares in a company, a business or assets be governed by local law?

The most important law regulating and governing private acquisitions and disposals in Japan is the Company Law (Law No.86 of 2005, as amended).

The following laws and regulations are also important:

- the Commercial Registration Law (Law No. 125 of 1963, as amended);
- the Law Concerning Prohibition on Private Monopoly and Preservation of Fair Competition (Law No. 54 of 1947, as amended) (Anti-monopoly Law); and
- the Foreign Exchange and Foreign Trade Law (Law No. 228 of 1949, as amended) (FEFT Law).

Share exchanges and corporate splits are statutory arrangements provided for by the Company Law, which is part of the laws of Japan. Therefore, the agreements or other documents for those transactions are required to satisfy the relevant requirements under, and be governed by, the laws of Japan. Agreements for share acquisitions and business transfers may be governed by the laws of any jurisdiction selected by the parties; however, in most cases, the agreements for those transactions are also governed by the laws of Japan.

3 What legal title to shares in a company, a business or assets does a buyer acquire? Is this legal title prescribed by law or can the level of assurance be negotiated by a buyer? Does legal title to shares in a company, a business or assets transfer automatically by operation of law? Is there a difference between legal and beneficial title?

Buyers acquire full legal title to shares in a company or a business, or assets. The concept of 'level of assurance' does not exist in Japan.

If a company is a company issuing share certificates, the shares in such company are transferred by delivery of the share certificates representing the transferred shares. Shares of a company not issuing share certificates are transferred as agreed upon between the seller and the buyer.

In the case of a business acquisition, the business or assets are transferred as agreed between the seller and the buyer; however, a transfer of contracts and liabilities is, in principle, subject to the consent of the counterparties or creditors. In the case of a corporate split, the business or assets are transferred, in principle, by operation of law.

There is a difference between a legal and beneficial title: the holder of legal title owns the shares or the assets, and is registered as the owner thereof, while the holder of beneficial title enjoys financial and other benefits.

4 Specifically in relation to the acquisition or disposal of shares in a company, where there are multiple sellers, must everyone agree to sell for the buyer to acquire all shares? If not, how can minority sellers that refuse to sell be squeezed out or dragged along by a buyer?

In the case of a share acquisition, a shareholder's consent is necessary to purchase the shares owned by such shareholder – that is, where there are multiple shareholders, the buyer cannot obtain all the shares unless all the shareholders agree to sell their own shares. However, where a small minority of shareholders refuse to sell their shares, the Company Law allows a shareholder holding 90 per cent or more of shares in a certain company (a target company) to squeeze out the minority shareholders by forcefully purchasing all shares held by such minority shareholders in the target company. This purchase of minority shareholders' shares may be done with the board approval of the target company and notification to such minority shareholders. By using this system, the squeezing out of the minority shareholders is, at the shortest, completed within approximately 20 days.

In the case of a share exchange, the Company Law authorises the use of straightforward squeeze-outs of minority shareholders through cash-out share exchanges. This transaction generally requires both board approval and supermajority shareholders' approval (two-thirds or more) of the companies concerned – the shareholders' approval is not required at the target company if the acquiring company already

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owns 90 per cent or more of the target company and at the acquiring company, depending on the significance of the transaction. One important caveat is that such squeeze-out transactions are required to be implemented on fair and commercially reasonable terms, otherwise the transactions may be challenged by the minority shareholders through an attempt to cancel the required shareholders' approval, etc.

5 Specifically in relation to the acquisition or disposal of a business, are there any assets or liabilities that cannot be excluded from the transaction by agreement between the parties? Are there any consents commonly required to be obtained or notifications to be made in order to effect the transfer of assets or liabilities in a business transfer?

In the case of a business transfer, in principle, the parties may choose the assets and liabilities to be transferred, and any asset or liability can be excluded from the transaction. However, in general, to transfer contracts (including employment contracts) and liabilities, the consent of the counterparty and the creditors, respectively, is required to be obtained.

In the case of a corporate split, in principle, the parties may choose the assets and liabilities to be transferred, and any asset or liability can be excluded from the transaction. The contracts are transferred by operation of law without consent of the counterparties; however, if there is a provision in such contract prohibiting the transfer by corporate split, the party would breach such provision by making the transfer, and would be liable to the other party for the breach. The liabilities are also transferred by operation of law without the consent of the creditors; however, the parties are required to conduct certain creditors' protection procedures. Under these creditors' protection procedures, the creditors are entitled to submit objections to the corporate split. Further, employees who are primarily engaged in the transferred business, and whom the parties agreed would be transferred, are transferred by operation of law without their consent. However, employees who are primarily engaged in the transferred business but will not be transferred, and employees who are not primarily engaged in the transferred business but will be transferred, are entitled to certain opt-out rights concerning their non-transfer or transfer, respectively.

6 Are there any legal, regulatory or governmental restrictions on the transfer of shares in a company, a business or assets in your jurisdiction? Do transactions in particular industries require consent from specific regulators or a governmental body? Are transactions commonly subject to any public or national interest considerations?

The Anti-monopoly Law generally prohibits acquisition of shares, acquisition of business or assets by corporate split, or acquisition of all or a substantial part of the seller's business by business transfer, as a result of which competition in certain fields or trades is substantially restrained.

Business combinations resulting in a foreign investor holding shares of other privately held Japanese companies will generally require a filing with the relevant ministries through the Bank of Japan under the FEFT Law. This filing is made ex post facto in most cases. However, where the target company is engaged in a certain category of business that raises national security or other public interest concerns (eg, military, aerospace, fishery, agriculture), prior notification is required to be filed. Regarding protected business areas among such categories (eg, fishery, agriculture), the prior filing requirement functions as a de facto ban.

In addition, acquisitions of shares, a business or assets in heavily regulated industries are sometimes subject to approval by the relevant authorities. A typical example thereof is the acquisition by a bank of certain businesses, which requires the Financial Supervisory Agency's approvals.

Other than the above, governmental agencies in Japan cannot influence or restrict the completion of business combinations. It should be noted, however, that in many cases, business combinations require commercial registration with the competent legal affairs bureau. The parties wishing to implement atypical business combinations may encounter objections from the officials of the legal affairs bureau when registering such atypical business combinations, and should therefore consult with the legal affairs bureau in advance.

7 Are any other third-party consents commonly required?

In cases where a parent company sells its subsidiary via a share acquisition, and the shares of such subsidiary are a substantial part of its assets (ie, the book value of the shares of the subsidiary to be sold exceeds one-fifth of the total assets of the parent company) such share acquisitions are required to be approved by a supermajority resolution of shareholders (which is the resolution adopted by an affirmative vote of at least two-thirds of the votes at a general meeting of shareholders, where the shareholders present at such meeting hold at least a majority (which resolution requirements and quorum requirements can be modified by the articles of incorporation to the extent permitted under the Company Law) of the relevant voting rights). For other cases, no such shareholder approval rights exist in the case of share acquisitions, except for some closed companies where the articles of incorporation of such companies so provide. However, as a matter of course, shareholders have a choice not to sell their own shares.

Share exchanges, corporate splits and business transfers (however, regarding a transferor, only in the case of a transfer of all or a substantial part of its business to another company, or, regarding a transferee, acceptance of all the business of another company) is required to be approved by a super majority resolution of shareholders. In small share exchanges and corporate splits below certain threshold requirements – as well as for shareholders' approval at a subsidiary in any of those business combinations, implemented with its 90 per cent or more parent company – this shareholders' approval is not required to be obtained.

8 Must regulatory filings be made or registration fees paid to acquire shares in a company, a business or assets in your jurisdiction?

Anti-monopoly Law

Under the Anti-monopoly Law, subject to certain threshold requirements and exceptions, if a company increases its shareholding in another Japanese or foreign company with a certain amount of sales in Japan, and the resulting shareholding ratio exceeds ownership thresholds of 20 per cent or 50 per cent, such company is required to file a prior notification with the Japan Fair Trade Commission, after which there is a 30-day waiting period.

Further, under the Anti-monopoly Law, subject to certain threshold requirements and exceptions, a company accepting a business transfer and a company implementing an absorption type corporate split are required to file a prior notification of such transaction with the Japan Fair Trade Commission, after which there is a 30-day waiting period.

FEFT Law

Under the FEFT Law, a foreign investor may be required to file ex post facto reports with the competent ministers through the Bank of Japan when it acquires shares of a Japanese company.

Stamp duty and other governmental fees

No stamp duty or other governmental fee is imposed on a share acquisition agreement or share exchange agreement. A stamp duty of ¥40,000 is imposed on a corporate split agreement. Stamp duty on a business transfer agreement varies depending on the price of the business being transferred, with the maximum amount being ¥600,000. A business combination often involves amendment of the company's commercial registration, which is subject to various registration taxes in amounts depending on the matters attached.

Advisers, negotiation and documentation

9 In addition to external lawyers, which advisers might a buyer or a seller customarily appoint to assist with a transaction? Are there any typical terms of appointment of such advisers?

Financial advisers and accountants are often retained by parties to assist them with a transaction. There appears to be no typical terms of appointment.

10 Is there a duty to negotiate in good faith? Are the parties subject to any other duties when negotiating a transaction?

Parties are subject to a general obligation under the Civil Code to act in good faith. The directors of a company owe a fiduciary duty to the company, and the Company Law also provides that the directors of a company are liable to third parties who suffer any damage due to wilful

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misconduct or gross negligence of such directors in the course of the performance of their duties as directors.

11 What documentation do buyers and sellers customarily enter into when acquiring shares or a business or assets? Are there differences between the documents used for acquiring shares as opposed to a business or assets?

Parties to a transaction to acquire shares, business or assets customarily enter into a confidentiality agreement to impose confidentiality obligations on each other concerning the information that they exchange between themselves, as well as the facts about the transaction itself; and a definitive agreement providing for the definitive terms and conditions of the transaction.

In the case of a share acquisition or business transfer, the definitive agreement is a sale and purchase agreement. In the case of a share exchange or corporate split, the parties are required to enter into a share exchange agreement or a corporate split agreement, respectively, which provides for certain items required under the Company Law. Since this agreement providing for statutorily required items has to be disclosed to, among other parties, creditors, if requested, in many cases the parties enter into another definitive agreement that provides for more detailed terms and conditions, such as representations and warranties or indemnifications.

Further, in some cases, the parties enter into a binding, or non-binding, MOU before negotiating the definitive agreements.

Except for the above, there is no substantial difference between the agreements to transfer shares (share acquisition or share exchange) or a business, or assets (business transfer or corporate split), provided that the agreements to transfer a business or assets identify the assets, liabilities, contracts and employees to be transferred to the seller.

12 Are there formalities for executing documents? Are digital signatures enforceable?

There is no formality required under the law for executing documents; however, in Japan, it is customary to affix seals of representatives of the company in executing documents. These seals are registered with the legal affairs bureau, and the party is sometimes required to submit the certificate of seal registry when executing the relevant documents.

Generally, digital signatures are enforceable under the law; however, it is uncommon to use digital signatures to execute documents in Japan.

Due diligence and disclosure

13 What is the typical scope of due diligence in your jurisdiction? Do sellers usually provide due diligence reports to prospective buyers? Can buyers usually rely on due diligence reports produced for the seller?

The scope of legal due diligence usually covers the following items:

- corporate structure, including articles of incorporation and other internal rules;
- validity of shares and shareholdings;
- transactions with affiliated companies;
- financing arrangements;
- assets, including intellectual properties;
- employee maters;
- agreements;
- licences and permissions;
- compliance with laws; and
- disputes.

It is uncommon in Japan for a seller to prepare a due diligence report for prospective buyers, or for a buyer to rely on a due diligence report prepared by a seller.

14 Can a seller be liable for pre-contractual or misleading statements? Can any such liability be excluded by agreement between the parties?

A seller may be liable for pre-contractual or misleading statements. However, such liability may be excluded by agreement, and the seller usually attempts to negotiate that the definitive agreement provides to such effect.

15 What information is publicly available on private companies and their assets? What searches of such information might a buyer customarily carry out before entering into an agreement?

The information registered in the commercial registry is publicly available on private companies, which includes:

- names of directors and statutory auditors;
- number and types of authorised shares and outstanding shares;
- amount of capital;
- whether or not the share certificates are issued;
- whether the approval of the company is necessary to transfer shares; and
- the date of incorporation.

In addition, information concerning the intellectual properties registered under the name of the company is searchable on the database provided by the Japan Patent Office. Further, detailed information concerning real estate owned by the company is also publicly available on the real estate registry.

Usually, during due diligence, the commercial registry of the target company is obtained to ascertain whether it is duly registered or verify other information. A determination of the issues of whether to search the intellectual properties held by the target company or confirm the real estate registries depends on the importance of such properties for the target companies, etc.

16 What impact might a buyer's actual or deemed knowledge have on claims it may seek to bring against a seller relating to a transaction?

In a decision of a lower court in Japan, it was determined that actual knowledge of a buyer, or knowledge that the buyer did not have because of its gross negligence, precludes a claim for breach of representations and warranties from being brought. In other words, the current understanding is that a party would be precluded from bringing such claim unless it is clearly excluded in the definitive agreement by a sand-bagging provision.

Pricing, consideration and financing

17 How is pricing customarily determined? Is the use of closing accounts or a locked-box structure more common?

For transactions of a certain scale, there are a number of cases in which a post-closing adjustment mechanism using closing accounts was provided, while there are many cases in which no post-closing pricing adjustment mechanism was adopted. The locked-box structure is not necessarily common in Japan.

18 What form does consideration normally take? Is there any overriding obligation to pay multiple sellers the same consideration?

While various types of consideration such as cash, shares and vendor notes are allowed, the consideration is usually cash.

There is no obligation to pay multiple sellers the same consideration in the case of a share acquisition. However, in the case of a share exchange, it is obligatory to distribute an equal amount of consideration based on the number of shares held by each seller (ie, the shareholders of the target company).

19 Are earn-outs, deposits and escrows used?

It is uncommon in Japan to use earn-outs, deposits or escrows.

20 How are acquisitions financed? How is assurance provided that financing will be available?

If the buyer is a private equity fund or the transaction is a management buyout, non-recourse loans are usually used, and if the buyer is an operating company, it is usual that recourse loans are used to fund the acquisition.

There is no specific rule in private M&A transactions on how to secure assurance of the financing, and this is left to the parties to determine. There are many cases in which the buyers obtain commitment letters from the banks and present them to the seller before executing the definitive agreement.

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21 Are there any limitations that impact the financing structure? Is a seller restricted from giving financial assistance to a buyer in connection with a transaction?

There is no legal limitation on financing structures, and there is no restriction in Japan on sellers giving financial assistance to a buyer. However, the target company in an M&A transaction should generally avoid offering its assets as collateral to secure acquisition finance for the acquirer in view of the interests of minority shareholders unless and until the target company becomes 100 per cent owned by the buyer as a result of the transaction.

Conditions, pre-closing covenants and termination rights

22 Are transactions normally subject to closing conditions? Describe those closing conditions that are customarily acceptable to a seller and any other conditions a buyer may seek to include in the agreement.

So long as the transaction has a certain scale, it is not unusual to set certain closing conditions to close the transaction.

Commonly accepted conditions are no material breach of representations and warranties, no material breach of covenants, obtainment of necessary regulatory approval (including expiration of a 30-day waiting period concerning filing under the Anti-monopoly Law) and completion of internal procedures. The buyer needs to negotiate if it wants to include no material adverse effect or other business conditions in the conditions precedent; however, there are many transaction documents in which these conditions are included.

23 What typical obligations are placed on a buyer or a seller to satisfy closing conditions? Does the strength of these obligations customarily vary depending on the subject matter of the condition?

There is typically a general provision under which each party is obligated to make reasonable efforts to satisfy the conditions. In addition, in connection with regulatory approvals, including antitrust filings, the party in charge of obtaining such approvals is subject to more detailed obligations to make efforts to obtain the same, and to an obligation to keep the other party informed of the process. Whether any other obligations are provided varies depending on the transaction.

The obligation to satisfy the conditions that may be controlled by the party, such as the condition to complete the internal process, is usually strong, and is provided as a definite obligation, while other obligations subject to the consent of third parties are usually provided as obligations to make reasonable efforts.

24 Are pre-closing covenants normally agreed by parties? If so, what is the usual scope of those covenants and the remedy for any breach?

Pre-closing covenants are normally agreed by the parties. The usual scope is to conduct the business in the ordinary course, to allow the buyer reasonable access to information about the company, to take necessary internal steps required for the transactions, to make reasonable effort to satisfy the conditions and other business matters (such as making reasonable efforts to obtain the consent of third parties, etc).

Remedies for the breach of covenants are usually to seek indemnification, to terminate the definitive agreement or not to close the transaction.

25 Can the parties typically terminate the transaction after signing? If so, in what circumstances?

In the case of typical transactions, if there is a material breach of covenants or representations and warranties, or the long-stop date has passed, the parties are entitled to terminate the transaction by terminating the definitive agreement.

26 Are break-up fees and reverse break-up fees common in your jurisdiction? If so, what are the typical terms? Are there any applicable restrictions on paying break-up fees?

To our knowledge, break-up fee arrangements have recently tended to be adopted more often than they were in the past, while reverse break-up fee arrangements are not yet very popular in Japan. However, there are no 'typical' terms for those fees.

Break-up fees and reverse break-up fees provided in the definitive agreements are generally enforceable in Japan, as long as the amount of the fees is reasonable in view of the costs and damage to the parties. If the amount of the break-up fee or the reverse break-up fee is unreasonably high, it is possible that a court might hold that the arrangement is contrary to public interest, and declare it null and void. Except for this, there are no applicable restrictions on paying break-up fees.

Representations, warranties, indemnities and post-closing covenants

27 Does a seller typically give representations, warranties and indemnities to a buyer? If so, what is the usual scope of those representations, warranties and indemnities? Are there legal distinctions between representations, warranties and indemnities?

A seller typically gives representations, warranties and indemnities for the breach thereof to a buyer. The scope of a seller's representations and warranties is usually as follows:

- capability and authority of the seller to enter into and perform the definitive agreement;
- due capitalisation and validity and legality of shares of the target company (particularly in the case of acquisition of shares);
- accuracy of financial statements;
- no undisclosed liability and no material changes;
- valid title to the properties;
- sufficiency of assets (especially in the case of acquisition of a business or assets);
- validity of contracts, etc;
- relation with affiliated parties;
- matters concerning employees;
- compliance with laws;
- due payment of tax;
- environmental issues;
- no legal proceedings; and
- no relationship with antisocial forces.

Under the laws of Japan, there is no clear distinction between representations and warranties, and indemnification is regarded as the monetary remedy in the case of a breach of representations and warranties.

28 What are the customary limitations on a seller's liability under a sale and purchase agreement?

The limitations on a seller's liability under the definitive agreement vary, and it is difficult to quantify them because, unlike in other jurisdictions such as the United States and the United Kingdom, there are no statistics in that regard for Japan. However, generally breaches of fundamental representations and warranties, such as the capability and authority of the seller to enter into a definitive agreement and the validity of the shares, are capped by the purchase price, while other representations and warranties are capped by a certain percentage (such as 10 to 25 per cent) of the purchase price. Further, provisions to limit a claim of a breach of representations and warranties only exists in cases where the amount of both an individual claim and also cumulative claims exceed a certain amount.

It is also common to set a survival period for a breach of representations and warranties other than the fundamental ones. The length of this period usually varies as well; however, it is usually around 18 months or less.

29 Is transaction insurance in respect of representation, warranty and indemnity claims common in your jurisdiction? If so, does a buyer or a seller customarily put the insurance in place and what are the customary terms?

Insurance for representations and warranties was introduced in Japan, and is used in some cases. However, such use is still uncommon.

30 Do parties typically agree to post-closing covenants? If so, what is the usual scope of such covenants?

Parties typically agree to post-closing covenants, such as a seller's post-closing covenants not to solicit the employees of the company and not to compete with the business of the company. Further, the seller sometimes agrees to maintain the terms of employment of, and keep

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employing, the employees of the company or transferred employees for a certain period of time (usually for one or two years).

Tax

31 Are transfer taxes payable on the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

In the case of transfers of shares of a Japanese private company, no transfer tax will be imposed. There is no financial transaction tax in Japan. Stamp duty is not imposed on a share purchase agreement.

If transfers of a business or assets are made by a company split (which is a statutory reorganisation transaction), stamp duty is imposed on the company split agreement at a rate of ¥40,000 per original copy, which is customarily borne by each party retaining such original copy. Registration and licence tax is imposed on the commercial registration of a company split at a rate of ¥30,000 for the transferring company and at a rate of 0.7 per cent of the increased amount of the stated capital (where the minimum rate is ¥30,000) for the succeeding company, which is customarily borne by each such company. When real property is transferred by a company split, real property acquisition tax is imposed in principle at a rate of three per cent or 4 per cent of the official appraised value of such real property; however, it is exempted in the case of a qualifying company split satisfying certain conditions. Registration and licence tax is also imposed on the real property registration of the transfer at a rate of 2 per cent of the official appraised value of such real property. This is customarily borne by the purchaser.

If transfers of a business or assets are made by a sale of a business or assets (which is an arbitrary sale agreement of a business or assets), stamp duty is imposed on the agreement on a sale of a business or assets per original copy at progressive rates depending upon the contract value, with the maximum rate being ¥600,000 if the contract value exceeds ¥5 billion. This is customarily borne by each party retaining such original copy. Real property acquisition tax and registration and licence tax are imposed if the transferred assets include real property, substantially in the same manner as a company split. However, there is no exemption of real property acquisition tax in the case of a sale of a business or assets. These taxes are customarily borne by the purchaser.

32 Are corporate taxes or other taxes payable on transactions involving the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

In the case of transfers of shares of a Japanese private company, income tax consequences will arise upon the capital gains (ie, the sale price or the fair market value of the shares minus the tax basis). If the seller is a Japan-resident individual, such capital gains are subject to income taxes at a rate of 20.315 per cent. If the seller is a Japanese corporation or a foreign corporation doing business through a permanent establishment in Japan, such capital gains are subject to corporate taxes at an effective rate of around 30 per cent to 34 per cent (with the rate depending upon the particulars of the seller). If the seller is a non-resident individual or a foreign corporation having no permanent establishment in Japan, capital gains arising from a transfer of a Japanese corporation (which is not a certain real property holding corporation, where special rules apply) are not in general subject to Japanese income taxation. This is not the case, however, where such foreign corporation or non-resident individual, together with certain related persons as defined in Japanese tax laws, owns or owned 25 per cent or more of the total shares of the Japanese corporation at any time during a period of three years on or before the end of the fiscal year of the foreign corporation (or the calendar year for non-resident individuals) in which the sale of such shares took place, and sells 5 per cent or more of the total shares of such Japanese corporation in that fiscal year or calendar year (the 25 per cent/5 per cent rule). However, the exemption may apply depending upon the capital gains article of the applicable tax treaty. No withholding tax applies to these capital gains taxation. These taxes are to be reported by the seller by filing a tax return, and are customarily borne by the seller. No Japanese consumption taxes or Japanese VAT are imposed on transfers of shares.

In the case of transfers of a business or assets (either by a company split or a sale) made by a Japanese corporation or by a foreign corporation doing business through a permanent establishment in Japan (by a sale only), the capital gains are subject to corporate taxes at an effective rate of around 30 per cent to 34 per cent (the rate differs depending upon the particulars of the seller). However, if such transfer is made by way of a company split constituting a tax-qualified company split satisfying certain conditions, the transfer can be made tax-free; that is, the capital gains taxation is deferred (which conditions, however, are unlikely to be met in the case of straightforward third-party acquisition deals). No withholding tax applies to such capital gains taxation. These taxes are to be reported by the seller by filing a tax return, and are customarily borne by the seller. Japanese consumption taxes, in the case of a sale of business or assets, will be imposed at a rate of 8 per cent (10 per cent from October 2019) on transfers of taxable assets (including goodwill associated with the business in the case of a Japanese corporation) in Japan. These consumption taxes are customarily borne by the purchaser, and are added on to the purchase price and paid by the seller to the government by filing a tax return. The purchaser is generally entitled to take input tax credit as to the consumption taxes so paid to offset against its own consumption tax liability. However, no Japanese consumption taxes will be imposed if the transfer is made by a company split, as this is not a taxable transaction.

Update and trends

During 2017, M&A activities in Japan were still very active, and it is reported that the number of acquisitions involving Japanese companies continued to increase in 2017. We would say that the increased number of small or mid-size transactions was one of the trends in 2017.

No significant change in legal or market practice in the private M&A transactions has been observed over the past 12 months.

Employees, pensions and benefits

33 Are the employees of a target company automatically transferred when a buyer acquires the shares in the target company? Is the same true when a buyer acquires a business or assets from the target company?

The employees of a target company are automatically 'transferred'; that is, such employees remain employed by the target company when a buyer acquires the shares in the target company.

If the business or assets are transferred by a business transfer, each individual employee's consent is necessary to transfer such individual. If the business or assets are transferred by a corporate split, it is unnecessary to obtain the consent of each individual employee; however, it is necessary to undertake certain procedures provided under the law. In addition, by corporate split, the employment terms applicable to the employees at the seller will be automatically and comprehensively succeeded by the buyer.

34 Are there obligations to notify or consult with employees or employee representatives in connection with an acquisition of shares in a company, a business or assets?

Unless there is a provision to that effect in a collective agreement with the labour union or other agreements, there is no need to notify or consult with employees or their representatives in the case of an acquisition of shares in a company or a business or assets, except for in the case of a corporate split. In the case of a corporate split, it is necessary to send notices to certain employees, as well as to consult with the labour union or, if there is no labour union, with the representatives of the employees.

35 Do pensions and other benefits automatically transfer with the employees of a target company? Must filings be made or consent obtained relating to employee benefits where there is the acquisition of a company or business?

In the case of a share transfer, pensions and other benefits are, in principle, automatically transferred with the employees (ie, they remain with the target company). However, it should be noted that, where the target company adopts the same pension and benefits system as its parent company (the seller), and needs to change them to be the same as those adopted by the buyer, there should be a procedure under which the pension system of the target company can be changed.

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In the case of an acquisition of a business, the necessary procedures all differ depending on the system adopted by the buyer and the seller. In the event that both the seller and the buyer adopt a defined contribution plan, the assets already contributed for the employees can be transferred without undertaking any procedure. However, in other cases, mostly the approval of authority (or at least, notification to the authority) and the consent of the employees would be required.

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