



Beyond Anglo-Saxon Models: Japan's Unique Approach to M&A and Its Impact on Shareholder Activism and Sustainability

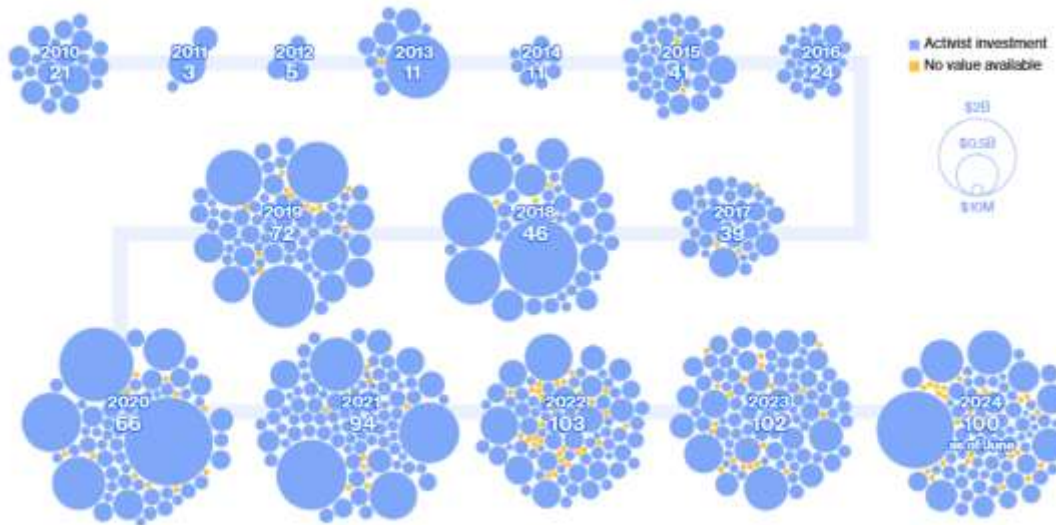
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Japan has Become World 's Second-biggest Market for Activists, Bloomberg (June 26, 2024)

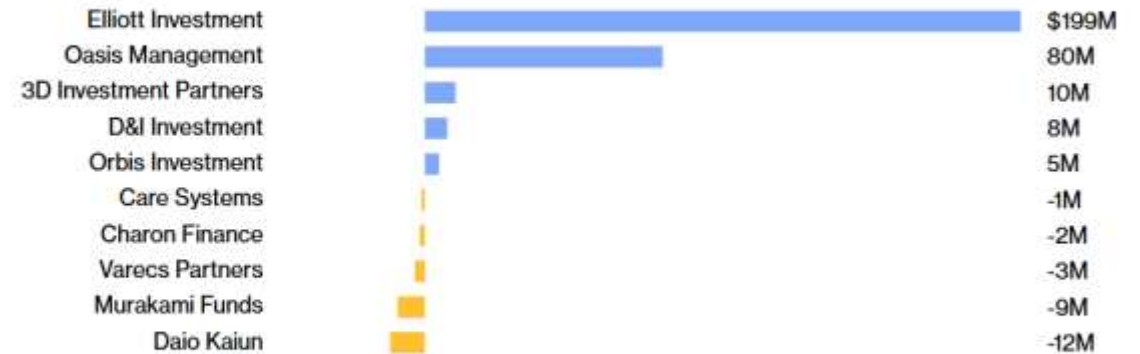
Number of Activist Investments Has Grown in Japan



Source: Data compiled by Bloomberg

Top and Worst 5 Performers

Returns from activist investment in Japan started in 2024



Source: Data compiled by Bloomberg
Note: As of June 25

Questions

1. Is the principle of shareholders' intent consistent with the corporate value standard?
2. Is it reasonable for Japanese law to generally permit partial acquisitions?
3. How is shareholder activism positioned under an M&A law?
4. How are the corporate value standard, the principle of shareholders' intent, and sustainability interrelated?

Japan has been evolving its M&A laws (1): Different from Delaware

Corporate Value Standard:

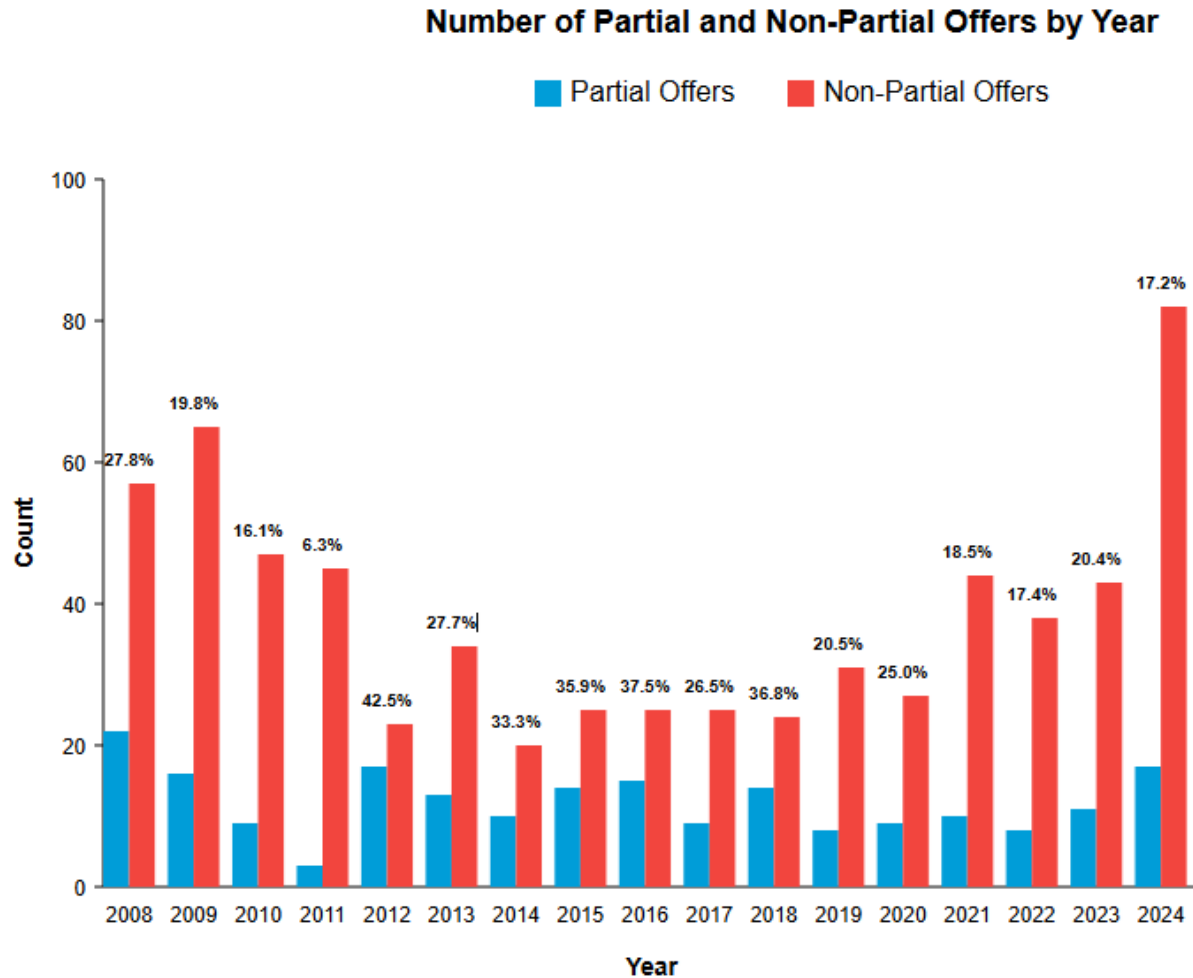
Whether an M&A transaction is considered 'good' or 'bad' is based on its potential to enhance corporate value, rather than solely on the acquisition price paid to shareholders

Principle of Shareholders' Intent:

Poison pills are available. Their triggering by the board of directors alone is likely to be enjoined by the courts, whereas shareholder approval significantly reduces the likelihood of such injunctions.

Compatible?

Japan has been evolving its M&A laws (2): Different from Europe



ワールド▼ マーケット▼ 経済▼ ビジネス▼ オピニオン▼ ライ

Itochu amasses 40 percent stake in Descente in rare Japan hostile bid

Ritsuko Ando

2019年3月15日 午後 5:30 GMT+9 - 6年前更新



The logo of Itochu Corp is seen outside the company's headquarters in Tokyo, Japan, November 7, 2016. REUTERS/Toru Hanai

Japan has been evolving its M&A laws (2): Different from Europe

- **Partial tender offers:**

- commonly used in Japan, both in friendly and hostile takeovers
- Available if upper limit is set under two-thirds of outstanding shares



Is it reasonable for Japanese law to generally permit partial acquisitions?

Reform of Tender Offer Rule (2024)

Before	Over 5%	Over 1/3	Over 1/2	2/3 or more
Off-market trades (10 or more shareholders)	TOB	TOB	TOB	(any and all) TOB
Off-market trades (less than 10 shareholders)		TOB		(any and all) TOB
Market trade				



After	Over 30%			
Off-market trades (10 or more shareholders)	TOB	TOB	TOB	(any and all) TOB
Off-market trades (less than 10 shareholders)		TOB	TOB	(any and all) TOB
Market trade		TOB	TOB	(any and all) TOB

KKR and Bain Capital competed in a takeover bid for FUJISOFT

time	KKR	Bain Capital	FUJISOFT Board of Directors' Recommendation
1	\8800		KKR
2		5% higher than KKR (non-binding offer)	KKR
3		\9450 (binding offer)	KKR
4	\9451		KKR
5		\9600	KKR
6	\9850	withdraw	KKR



Corporate Value and Offer Price

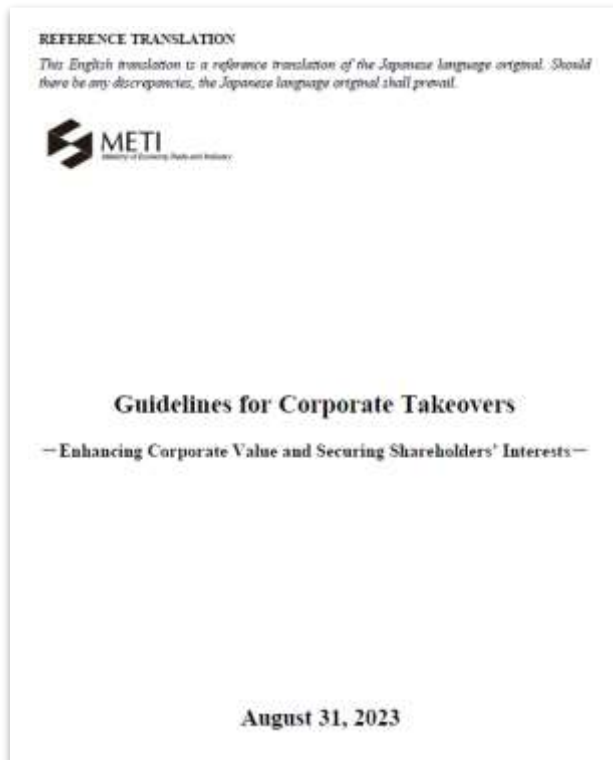
- Do directors breach duties by accepting a lower offer when multiple takeover bids exist?
- No. Directors may select an offeror who better enhances corporate value.
 - Primary: Will the acquisition increase overall corporate value?
 - Secondary: Is the offer price fair?

METI, Guidelines for Corporate Takeovers (2023)

Principle 1: Principle of Corporate Value and Shareholders' Common Interests

Whether or not an acquisition is desirable should be determined on the basis of whether it will secure or enhance corporate value and the shareholders' common interests.

“Corporate value” refers to a company's assets, profitability, stability, efficiency, growth potential, and other company attributes that contribute to the interests of shareholders, or the extent to which they do so. Conceptually, corporate value is the sum of the present values of discounted future cash flows generated by a company.



Shareholders are interested in offer price, but not corporate value after a takeover

- Shareholders' perspective:
 - Primary concern: Acquisition price (high vs. low)
 - Generally unconcerned with post-acquisition corporate value changes
- Principle of Shareholders' Intent:
 - Shareholders prefer higher offers regardless of corporate value impact
 - Board cannot override shareholder-approved offers
- Key question: Is Corporate Value Principle compatible with Shareholders' Intent Principle?

Higher offer price, because bigger synergies

- Higher acquisition price typically reflects higher expected corporate value
- Hypothetical scenario (all-or-nothing offers):
 - Raider A: Increases company value by 100
 - Raider B: Increases company value by 50
 - A can offer up to 100
 - B can offer only up to 50
 - Result: Shareholders naturally choose A's higher offer
- Conclusion: Even when shareholders focus solely on price, their decisions often align with corporate value standard

When the best acquisition price does not coincide with maximizing corporate value

- Hypothetical scenario (all-or-nothing offers):
 - Target current share price: ¥100
 - Raider A: Adds value of 100, offers ¥200
 - Raider B: Adds value of 50, offers ¥250
 - Shareholders choose B's higher offer
- Possible explanations:
 1. B is overconfident about value creation potential (150 vs. actual 50)
 2. B faces competitive disadvantage (-200) if A acquires target
 3. B plans to extract value from stakeholders (e.g., employees)

Combination of Principles of Corporate Value Standard and Shareholders' Intent as Second Best

- Target company's board:
 - 1. Should base takeover decisions on corporate value
 - 2. Cannot block shareholders from accepting offers in their interest
- Not ideal: Cases exist where highest price doesn't maximize corporate value
- Risk: Allowing board discretion for countermeasures could create greater inefficiency due to conflicts of interest

Corporate value standard is better than offer price standard

- Takeover desirability should be evaluated by corporate value standard
 - Corporate value assessment can be objective through:
 - Financial adviser's fairness opinion
 - Special committee and Court scrutiny
- Under offer price standard:
 - Higher price = more desirable acquisition
 - But higher price benefits target shareholders at acquirer's expense
 - No increase in net economic benefit (welfare)

Principle of Shareholders' Intent serves as a safety valve against directors abusing their power

- Risk of board authority: Directors may invoke "corporate value" as pretext to reject takeovers while actually preserving their positions
- Shareholders' Intent Principle serves as safety valve:
 - Prevents directors' abuse of power
 - Preserves shareholders' final decision right on takeovers

Reform of Tender Offer Rule (2024)

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Market trade		TOB	TOB	(any and all) TOB

The Financial System Council, The Working Group on Tender Offer Rule and Large Shareholding Reporting Rule, Report (2023)

“In European countries, tender offer rules are considered to ensure opportunities for minority shareholders to sell their shares at fair prices at the time of transfer of control, and thus, the following are adopted:

- rules that require tender offers to be made in principle after the event when a specified threshold for beneficial ownership ratio is exceeded regardless of the type of transactions;
- ban on partial tender offers, in principle; and
- minimum price rules.

This working group considered whether Japan’s tender offer rule should shift to a European-style rule.”

The Financial System Council, The Working Group on Tender Offer Rule and Large Shareholding Reporting Rule, Report (2023)

- Pros

such a rule

- has clear regulatory purposes and discipline that is fully consistent with the purposes
- provides especially ample protection for general shareholders,
- can have the effect of curbing structural conflict of interest between controlling shareholders and minority shareholders from occurring

- Cons

- the shift to the European-style rule would need a structure that flexibly allows exceptions to avoid undermining sound M&A deals (an organization that has expertise and flexibility)
- we should reach a conclusion after considering a broad range of options for the protection of minority shareholders, including related rules (e.g. fiduciary duties of controlling shareholders, sellout right of minority shareholders, duties of neutrality of directors)

Conclusion: a shift to a European-style rule should not be carried out immediately

Discussion of Partial Tender Offers

- Pros
 - Cost of finance
 - Keep a target company listed
 - Due Diligence Opportunity for a Hostile Bidder
- Cons
 - Inefficient Takeovers Might Succeed
 - May harm minority shareholders

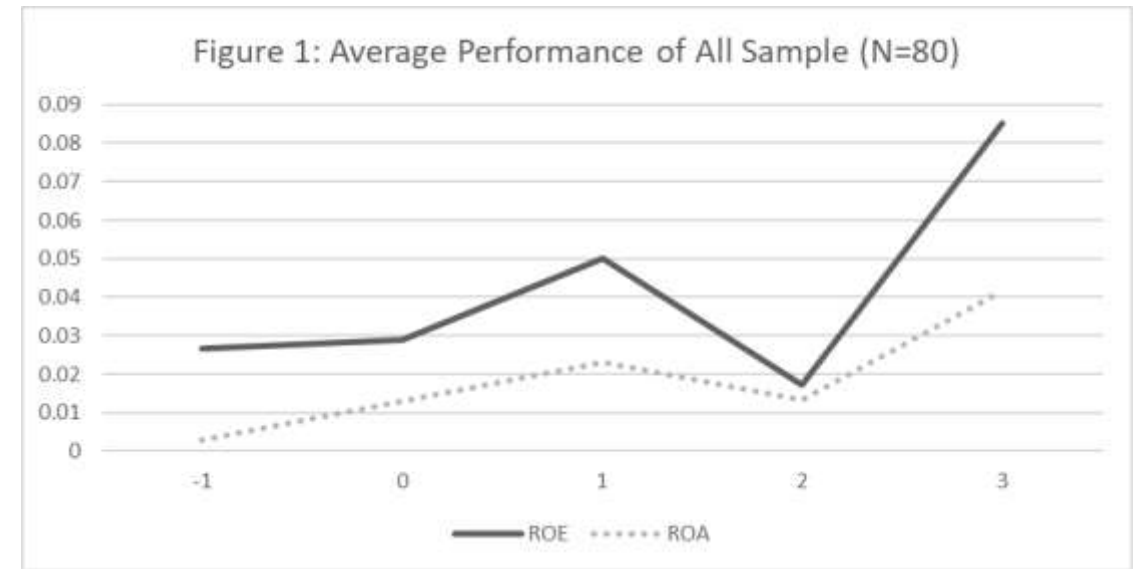
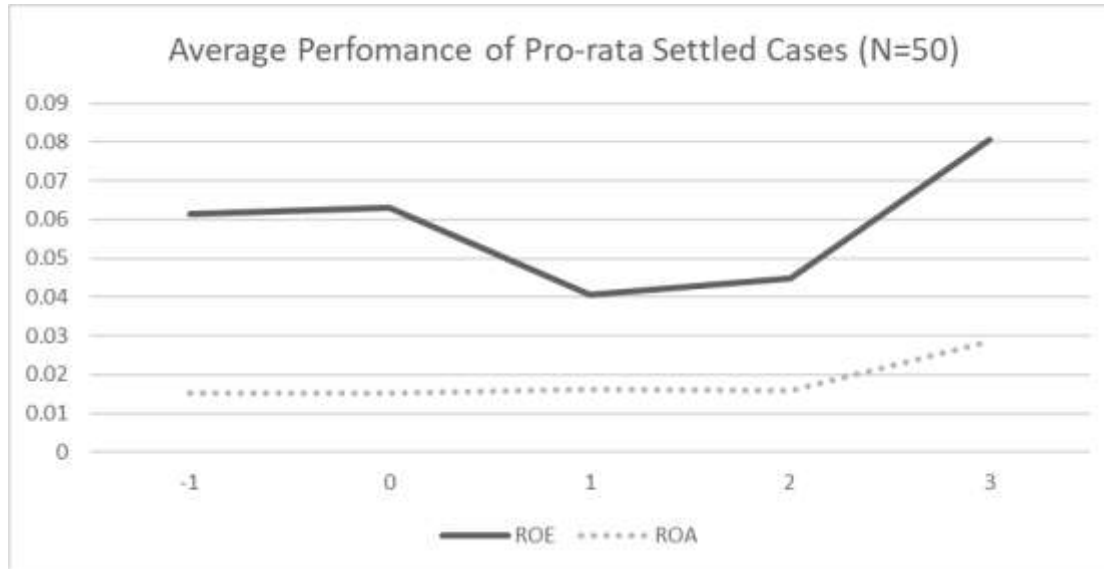
Table 1: Partial Tender Offers Premium

Variable	Obs	Mean	Std. Dev.	Min	Max
A. All Sample					
Premium to 1 day before	196	17.87	32.51	-90.30	180.64
Premium to 1 month before	196	18.74	33.00	-91.11	185.62
Premium to 3 months before	196	19.43	33.35	-91.24	183.85
Premium to 6 months before	196	18.50	34.79	-91.27	194.87
B. Pro rata settled cases					
Premium to 1 day before	125	24.72	25.15	-31.29	118.75
Premium to 1 month before	125	25.93	25.00	-16.47	118.07
Premium to 3 months before	125	25.99	25.51	-15.82	113.52
Premium to 6 months before	125	24.39	24.87	-22.71	116.29

Table 2: Market-Adjusted Return of Target Companies after Partial Tender Offers

Variable	Obs	Mean	Std. Dev.	Min	Max
A. All Sample					
Return 1Y	118	0.112 ***	0.444	-0.948	1.842
Return 2Y	118	0.262 ***	0.787	-0.978	5.319
Return 3Y	118	0.557 ***	1.631	-0.995	13.602
Market Adjusted Return 1Y	118	0.056	0.372	-0.710	1.337
Market Adjusted Return 2Y	118	0.120 *	0.732	-1.106	4.634
Market Adjusted Return 3Y	118	0.299 **	1.615	-1.853	13.428
B. Pro rata Settled cases					
Return 1Y	72	0.057	0.356	-0.948	1.155
Return 2Y	72	0.189 ***	0.602	-0.978	1.994
Return 3Y	72	0.597 ***	1.870	-0.995	13.602
Market Adjusted Return 1Y	72	0.034	0.307	-0.679	0.991
Market Adjusted Return 2Y	72	0.096	0.576	-0.768	2.041
Market Adjusted Return 3Y	72	0.403 *	1.866	-0.802	13.428

***, **, and * indicate statistical significance at 1% , 5% , and 10% level, respectively.



Discussion

- No evidence supports complete prohibition of partial offers under corporate value standard
- Controlling shareholders:
 - May expropriate assets, disadvantaging minorities
 - But "control change = minority disadvantage" theory doesn't always hold
 - Can have both positive and negative effects
- Case-by-case approach preferred over blanket prohibition-
- Poison pills are underinclusive (used only against hostile bids)
- Recommendation: Allow shareholders to convene meetings to vote on partial takeover bids

Anti-Activist Pill will not come to Japan (?)

- No documented cases of Japanese companies using defense measures with low triggers (5-10%)
- Japanese case law:
 - Permits poison pills if acquirer would damage corporate value
 - Courts value shareholder approval as evidence of potential damage
- Activist acquiring 10% stake:
 - Does not equate to gaining control
 - Target cannot claim value impairment based solely on activist proposals

Impact on Sustainability

- Sustainability factors (human capital, environment):
 - Not direct criteria for acquisition desirability
 - Relevant only through impact on corporate value (cf. single materiality)
- Board cannot introduce defensive measures solely to protect stakeholder interests
- Sustainability management survives only with shareholder support
- If shareholder support inadequate:
 - Direct regulatory approaches needed
 - Example: Carbon emissions regulations

Conclusion

- Japanese law's rationality:
 1. Combines corporate value standard with shareholders' intent principle
 2. Permits partial tender offers (flexible approach)
- Japan follows distinct third path from US and European models
- Conclusion: This balanced approach is rational