

# market intelligence

GETTING THE  
DEAL THROUGH 

## M&A

2018 – the return of  
the ‘mega-deal’

*Global interview panel  
led by Alan Klein*

# 2018

North America • Asia-Pacific • Europe • Latin America  
Keynote deals • Sector focus • Shareholder activism • 2019 outlook

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# market intelligence

Welcome to GTDT: *Market Intelligence*.

This is the 2018 edition of *M&A*.

**Getting the Deal Through** invites leading practitioners to reflect on evolving legal and regulatory landscapes. Through engaging and analytical interviews, featuring a uniform set of questions to aid in jurisdictional comparison, *Market Intelligence* offers readers a highly accessible take on the crucial issues of the day and an opportunity to discover more about the people behind the most interesting cases and deals.

*Market Intelligence* is available in print and online at  
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# M&A IN JAPAN

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He was admitted to the Japanese Bar in 2005 and in New York in 2011. He is recognised as one of the leading M&A lawyers in *Who's Who Legal: Japan 2017*.

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M&A transactions (involving listed and private companies); matters involving corporate governance, shareholder activism, proxy fights, unsolicited takeovers and takeover defence; and general corporate and securities law matters.

He was admitted to the Japanese Bar in 2006 and the New York Bar in 2013. He received his LLB from Keio University in 2005 and his LLM from Cornell Law School in 2012. He also worked at Kirkland & Ellis LLP, Chicago, from 2012 to 2013. He has published 'M&A Contract – Model Clauses and Commentary', 'Comprehensive Analysis of M&A Laws of Japan', 'TOBs in Japan – Systems and Demonstrations', 'Shareholders' Proposal and Proxy Fight' and the Japan chapter in *The Shareholder Rights and Activism Review*.



**GTDT:** *What trends are you seeing in overall activity levels for mergers and acquisitions in your jurisdiction during the past year or so?*

**Kenichi Sekiguchi and Akira Matsushita:**

Appetite for M&A transactions continues to grow and the M&A market in Japan has been quite active in 2017 and the first half of 2018. The number of M&A transactions involving a Japanese company hit a record high in 2017 and the first half of 2018 recorded a more than a 30 per cent increase in terms of the number of deals as compared with the first half of 2017.

Outbound M&A transactions continue to increase as can be seen in Takeda Pharmaceutical's announcement to acquire Shire at US\$62 billion.

In the Japanese market, there were many divestment transactions by Japanese conglomerates as they continued to implement their strategies of focusing on their core competencies, while Toshiba was forced to divest many of its subsidiaries and other assets because of financial problems.

Private equity in Japan has been quite active as some major Japanese private equity firms successfully launched new funds and obtained additional funding from a variety of investors. International private equity firms have also successfully completed a few sizable transactions in Japan. Bain Capital led a consortium and acquired Toshiba Memory Corporation at approximately US\$18 billion. It also acquired Asatsu-DK, Japan's third-largest ad agency, at US\$1.4 billion through a tender offer and a subsequent squeeze-out process. On the other hand, in 2017, KKR acquired Calsonic Kansei, a Tier 1 auto parts supplier that was a subsidiary of Nissan Motors and two Hitachi listed subsidiaries, Hitachi Kokusai and Hitachi Koki.

Driven by some major transactions by Bain and KKR, as well as Key Safety Systems' acquisition of Takata's airbag business, 2017

saw the highest level of inbound investments since 2001.

In recent years, M&A has become a viable option for start-ups and we have seen many such transactions.

**GTDT:** *Which sectors have been particularly active or stagnant? What are the underlying reasons for these activity levels? What size are typical transactions?*

**KS & AM:** For outbound M&A transactions, the most active sectors are technology, media and telecommunications (TMT), life and non-life insurance, consumer and pharmaceutical.

After the acquisition of ARM Holdings in 2016 at US\$31.8 billion, which broke the then-record for the deal size of outbound M&A transactions by Japanese companies, Softbank has continued its deal-making, including transactions through the Softbank Vision Fund, which has major investors such as the Saudi government and has US\$100 billion of committed capital. Among the top 20 deals in terms of deal size that occurred in 2017, Softbank was involved in six including investment in Xiaoju Kuaizhi, Grab and WeWork.

In the insurance sector, we have seen a series of sizeable transactions in recent years. Since 2015, there have been nine M&A transactions by Japanese insurance companies exceeding approximately US\$10 billion, seven of which were outbound transactions. In the non-life insurance sector, Sampo Holdings acquired Endurance at US\$6.3 billion in 2016, while its rival MS&AD Insurance Group Holdings acquired Amlin in 2015 at US\$5.3 billion and First Capital, a Singapore-based non-life insurance company, at US\$1.6 billion in 2018. Life insurance companies have also been active in recent years, as shown by Nippon Life's acquisition of MLC at US\$2.2 billion, which was completed in October 2016 and its recent acquisition of MassMutual Japan at US\$0.93 billion, which was completed in May 2018. The Japanese insurance market is



already mature, and in light of Japan's ageing and shrinking population, room for domestic growth is quite limited. Therefore, going abroad for growth is an inevitable trend for insurance companies.

**GTDT: What were the recent keynote deals? What made them so significant?**

**KS & AM:** The acquisition of Toshiba Memory Corporation in June 2018 by a consortium led by Bain Capital together with a group of Japanese, US and Korean companies was a notable transaction, not only because of its deal size but also the complexity of the transaction structure as well as the circumstances leading up to its completion.

Toshiba was faced with financial problems and decided to divest its crown jewel: the semiconductor memory business. This business was so attractive that many industrial and financial players expressed interest. The transaction also attracted the attention of the Japanese government as it may result in mass lay-off or leakage of important technology.

Initially, Western Digital, a US company, had been said to be the most prominent bidder as it had an existing joint venture with Toshiba and certain veto rights were arguably granted under the relevant agreement. After a series of discussions with various interested parties, however, Toshiba ultimately decided to sign a definitive agreement with the consortium led by Bain Capital.

Western Digital initiated an injunction to prevent Toshiba from disposing the semiconductor memory business based on its veto rights under the joint venture agreement. While an injunction for an M&A transaction is not quite common in Japan and the decision of the arbitration tribunal was awaited, the case was finally settled in an amicable manner. To address Western Digital's concern, according to public information, the consortium agreed in the settlement to restrict access to certain confidential information of the semiconductor memory

business by one of the consortium members, SK Hynix, Western Digital's Korean competitor. In addition, Bain Capital agreed to allow the Japanese companies to hold the majority of votes so that the clearance of the Japanese government would be smoothly obtained.

**GTDT: In your experience, what consideration do shareholders in a target tend to prefer? Are mergers and acquisitions in your jurisdiction primarily cash or share transactions? Are shareholders generally willing to accept shares issued by a foreign acquirer?**

**KS & AM:** While cash is more commonly used as consideration in acquisitions, the type of consideration varies depending on the nature and structure of the acquisition. In a share purchase or business transfer, the consideration is predominantly cash only. An exchange offer through which the acquirer offers its own securities as consideration in a tender offer is legally permitted but the use of exchange offers had not developed in practice in Japan until recently because capital gain taxes could not be deferred in the case of an exchange offer. Due to recent regulatory changes, we hope to see more exchange offers.

In a statutory business combination – such as a merger, share exchange or company split involving a listed company – stock is more commonly used as consideration, although cash or other consideration is legally permitted and is often seen in the case of a company split.

Considerations comprised of a mix of cash and stock are not common in Japan, although such a mix is legally permissible. However, a cash tender offer followed by a second-step stock-for-stock merger or share exchange is often seen, and this structure effectively provides the shareholders with both cash and stock.

Japanese shareholders are not generally willing to accept shares issued by a foreign acquirer because access to information about the foreign



“Cash-out mergers or share exchanges may become options for conducting a squeeze-out of minority shareholders.”

acquirer would likely be limited for most domestic shareholders. If shares of a foreign acquirer are issued to shareholders of a listed company, the foreign acquirer must file a security registration statement in Japan.

*GTDT: How has the legal and regulatory landscape for mergers and acquisitions changed during the past few years in your jurisdiction?*

*KS & AM:* As a result of the tax reform implemented in 2017, a tax qualified treatment has become available for a cash-out merger or share exchange if the surviving company or parent company holds at least two-thirds of the total outstanding shares of the disappearing company or subsidiary company and other requirements are met. Thus, cash-out mergers or share exchanges may become options for conducting a squeeze-out of minority shareholders. Also, as a result of the 2017 tax reform, squeeze-out transactions are treated as reorganisations under the Japanese Corporate Tax Act, under which a target company would be subject to corporate tax on built-in profit or loss of its assets, in a transaction which does not meet the tax qualified requirements. In addition, if a squeeze-out transaction, in which a company that adopts the consolidated taxation system makes a target a wholly owned subsidiary, meets the requirements of the tax qualified treatment, taxation on built-in profits or losses of assets of the target can be avoided and net operating loss carry forward of the target can be used in the target even after the transaction.

During 2018, the Act on Strengthening Industrial Competitiveness (the ASIC) was amended. Prior to the amendment, the exemptions from certain regulations under the Companies Act for M&A transactions for using acquirer's shares as consideration was available only for an exchange tender offer. After the amendment, such exemptions (for using acquirer's shares as consideration) became available for any acquisitions which meet certain requirements under the ASIC. In addition, as explained above, exchange tender offers and other share-for-share acquisitions other than statutory business combinations, such as mergers and share exchanges, had not been used by acquirers because capital gain taxes owed by shareholders of a target company could not be deferred. The tax reform implemented in 2018 permits tax deferral for a share-for-share acquisition, other than statutory business combinations, of controlling shares in a target pursuant to a 'special business restructuring plan' approved by the competent minister under the ASIC, if such acquisition meets certain requirements. A special business restructuring plan is required to be a plan in which a Japanese joint-stock corporation, that is the acquirer, will achieve considerable improvement to its productivity as a result of new demands

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through the establishment of specific new business activities. The tax deferral is not available for transactions in which the consideration consists of a mix of shares and cash.

Additionally, the interim proposal for the Companies Act Revision, released by the Legislative Council of the Ministry of Justice on 28 February 2018, proposes to introduce new rules regarding a method of delivery of shares known as 'Share Delivery', under which an acquiring company may deliver its shares to shareholders of a target as consideration for an acquisition of the target's shares, held by such shareholders, to make the target a subsidiary of the acquiring company. The bill to amend the Companies Act is expected to be submitted to the Diet in early 2019 at the earliest.

Furthermore, the 2017 tax reform permits deferral of taxation arising from certain spin-off transactions in which a part of a company's business, or its wholly owned subsidiary, is carved out and shares in such business or wholly owned subsidiary are distributed to the company's shareholders pro-rata through a dividend in kind. Under the ASIC amended in 2018, a company with articles of incorporation that authorise its board of directors to distribute dividends may spin-off its business by distribution in kind without obtaining approval by a special resolution at its shareholders meeting, pursuant to a business restructuring plan approved by the competent minister if shares of the company that is spun off are scheduled to be listed on the stock exchange without delay. These amendments may increase the options available for a company to structure a carve-out of a part of its business.

**GTDT: Describe recent developments in the commercial landscape. Are buyers from outside your jurisdiction common?**

**KS & AM:** In the Japanese M&A market, outbound cross-border M&A transactions continued to be very active during 2017 and into 2018. In particular, the number of outbound M&A transactions in 2017 stands at a record high. Since the domestic market in Japan has not been expected to grow much, many Japanese companies have decided during this decade to expand their businesses and to find new opportunities in the growing markets in Asia, and this trend has continued in 2017. Furthermore, a number of investments in start-up companies have been made by listed companies in Japan for the purpose of seeking new business opportunities, and such investments have rapidly increased during the past several years.

On the other hand, the number of sales of foreign subsidiaries or assets by Japanese companies have also increased. While a lot of Japanese companies have actively engaged in outbound M&A transactions during this decade, some of these companies have needed

to rationalise their foreign businesses to adapt to changes in the business environments of global markets.

Looking to the Japanese domestic market, foreign private equity funds have continued to actively engage in M&A activity in Japan during 2017 and into 2018; with the number of large value deals having noticeably increased during this time. For example, the acquisition of Toshiba Memory by Bain Capital and its co-investors was the largest M&A transaction in Japan during 2017. The acquisition of Hitachi Kokusai Electric by KKR and the Japanese private equity fund, Japan Industrial Partners, the acquisition of Asatsu-DK by Bain Capital and the acquisition of Hitachi Koki by KKR are also ranked in the list of large value M&A transactions in Japan during 2017.

**GTDT: Are shareholder activists part of the corporate scene? How have they influenced M&A?**

**KS & AM:** The influence of shareholder activists has increased in the corporate scene in Japan during the past several years for a variety of reasons. Institutional investors have become more actively engaged with their investee companies, and their voting judgments have become more stringent in light of the Japan's Stewardship Code, which was amended on 29 May 2017. Moreover, the number of cross-shareholders who vote in shareholder votes in support of the management of listed companies has decreased, and such decrease in cross-shareholders is supported by the Japan's Corporate Governance Code which was amended on 1 June 2018. As an example of the trend of shareholders in Japan becoming more comfortable with, and supportive of, shareholder activism, at the annual shareholders' meeting of Kuroda Electric in June 2017, a shareholder proposal made by an activist fund to elect an outside director designated by the activist fund was approved.

The number of M&A transactions involving shareholder activism has been increasing, especially in transactions involving conflicts of interests between an acquirer and minority shareholders, such as in transactions involving squeeze-outs of minority shareholders in listed subsidiaries by parent companies. Some shareholder activists have expressed their views regarding such transactions through public campaigns or in private discussions, and have stated that the transaction considerations are lower than fair value, and demand that the buyers or companies increase such considerations. For instance, a Hong Kong-based activist fund, Oasis Management, engaged in public campaigns with respect to the acquisition by Panasonic of its listed subsidiary, PanaHome, in 2017 and the acquisition by Alps Electric of its listed subsidiary, Alpine, which will be effective on 1 January 2019. In another example, KKR increased the tender offer

# THE INSIDE TRACK

## *What factors make mergers and acquisitions practice in your jurisdiction unique?*

Typical M&A practices and processes in Japan are generally not so different from those of the United States and Europe. The main transaction agreements in M&A transactions, such as stock purchase agreements and shareholder agreements, including with respect to the scope and content of their provisions, are generally similar to the agreements utilised in M&A transactions in the US and Europe. Of course, as with all jurisdictions, parties conducting transactions in Japan should take note of some local rules particular to Japan, such as with respect to certain restrictions on layoffs under the labour laws and the company governance requirements under the Companies Act.

One noteworthy factor is that few hostile takeovers have been successfully completed in Japan, partly because the identity of shareholders in listed companies has been quite stable and public opinion in Japan has been generally against hostile takeovers. Also, counter-proposals against a disclosed transaction have rarely been made by third-party bidders in Japan. However, in the event that cross shareholdings in Japanese companies dramatically decrease in the future due to the new corporate governance rules, more cases of hostile takeovers or counter-bids could potentially occur.

## *What three things should a client consider when choosing counsel for a complex transaction in your jurisdiction?*

First, a law firm should be able to set up a suitable team composed of a variety of relevant specialists, because a complex transaction usually requires a wide range of expertise. Since prompt attention and support is necessary in such transactions, and due to the volume of work, such as in due diligence and the preparation of transaction documents, the size and resources of the firm are also important considerations.

Second, it is important for a client that a counsel is not only competent in ability and experience; the counsel should also have the right mentality and business judgement to seek true

understanding of the needs and goals of the client in order to provide the best solution and advice for the client.

Third, a client should confirm which lawyers in the transaction team will actually handle or serve as the point persons for the transaction. To successfully complete a complex transaction, reliable lawyers must be heavily involved in the transaction including maintaining good and regular communications with the client.

## *What is the most interesting or unusual matter you have recently worked on, and why?*

We represented Jupiter Telecommunications, the largest Japanese cable TV operator, in its going-private transaction by KDDI and Sumitomo Corporation. The transaction was a two-step, going-private transaction involving a tender offer and subsequent statutory squeeze-out process. The transaction was announced in October 2012 and the tender offer commenced in February 2013 because it took a few months for the buyers to complete merger filings in China. The squeeze-out became effective in early August 2013. During this period, because of a series of new economic policies implemented by the then newly inaugurated Prime Minister Shinzō Abe, the Japanese stock market recorded a significant rise. Foreign institutional shareholders claimed that the tender offer price was too low considering the general changes of the market condition and initiated appraisal court proceedings.

After lengthy proceedings through the District Court and the High Court, we were able to successfully obtain a decision from the Supreme Court clarifying that the court's review in appraisal proceedings should focus on procedural fairness.

The transaction and subsequent appraisal proceedings were interesting because they include various implications that may affect the practice of going-private transactions in Japan including how the parties should manage conflict-of-interest issues.

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price by 25 per cent for the acquisition of Hitachi Kokusai Electric as a result of the purchase of a large amount of shares in Hitachi Kokusai Electric by Elliott Management after the announcement of the acquisition. Given recent trends, management of listed companies should appropriately take into account potential reactions and actions of shareholder activists when conducting M&A transactions.

In addition, in relation to a certain type of M&A transactions, shareholder activists may exercise, and some have exercised, their appraisal rights as dissenting shareholders to file a petition to the court for a determination of the fair price of the relevant shares after the completion of the M&A transaction.

**GTDT: Take us through the typical stages of a transaction in your jurisdiction.**

**KS & AM:** M&A transactions are typically initiated either by discussions between managements of the seller and buyer or contacts by a financial adviser to a potential seller or buyer depending on the particulars of the transactions, such as transaction value, relationships between the parties or the industries and businesses of the target companies. Sellers often implement an auction process to find a buyer as this process often results in a higher purchase price. Negotiating with more than one potential buyer in an auction process may also give a seller a bargaining advantage to negotiate more favourable terms

and conditions for the seller in the definitive transaction agreements.

A seller and potential buyers usually execute non-disclosure agreements, after which the seller provides the potential buyers with fundamental information regarding the target. A seller and a buyer sometimes enter into a memorandum of understanding, often legally non-binding, before proceeding to the due diligence phase.

An auction process typically has two stages. In the first stage, potential buyers are usually provided with an information package prepared by the seller. After the potential buyers review the information and perhaps after conducting preliminary due diligence, they submit bid letters stating their preliminary offer prices to the seller. The seller then selects a few preferred potential buyers to proceed to the second stage in which further due diligence is conducted and the parties negotiate the transaction agreements. A buyer often requests that a seller or target give the buyer exclusivity in the negotiation of a transaction before due diligence because the buyer wants to avoid spending unnecessary costs and resources for due diligence and evaluation of the transaction.

In many large cases, documents for the due diligence are provided to potential buyers through a virtual data room. It is also common for potential buyers and their advisers to hold some interview sessions with the target during the course of their due diligence of the target. Due diligence procedures have become more efficient and streamlined in recent years, such that the time required by parties to complete due diligence has become shorter than in the past.

**GTDT: Are there any legal or commercial changes anticipated in the near future that will materially affect practice or activity in your jurisdiction?**

**KS & AM:** As mentioned earlier, shares of a listed company may be used as consideration in a tender offer, but the use of shares as consideration had not been used for tax reasons. Because of the recent regulatory reforms, subject to satisfaction of certain conditions, the deferral of capital gain taxes in share-for-share tender offer transactions is now permissible.

The amendment to the Civil Law (Act No. 44 of 2017) was promulgated on 2 June 2017 and will be effective on 1 April 2020. However, this amendment is not expected to materially affect M&A practices in Japan, although legal practitioners should take it into account when advising their clients.

**GTDT: What does the future hold? What activity levels do you expect for the next year? Which sectors will be the most active? Do you foresee any particular geopolitical or macroeconomic developments that will affect deal sizes and activity?**

**KS & AM:** When considering an acquisition, management is always concerned about possible goodwill impairment. Such sentiment was fuelled by the recent goodwill impairment by Japan Post Holdings arising from its acquisition of Toll Holdings in the amount of US\$3.6 billion. Toshiba also disclosed huge goodwill impairment related to its US nuclear power plant construction business, CB&I Stone W Webster, which was acquired for US\$229 million in late 2015 by Toshiba's subsidiary, Westinghouse.

Nevertheless, faced with an ageing population and a shrinking domestic market, Japanese companies will have no choice but to look into foreign markets for growth. Therefore, we expect that the trend of increasing outbound M&A transactions will continue. As mentioned earlier, the TMT, insurance, consumer and pharmaceutical sectors will continue to be the main areas for M&A growth.

Domestic M&A transactions will also likely continue to increase. The Japanese government has been trying to improve the corporate governance of Japanese companies and, although still far from the activity level in the United States, shareholder activism is becoming less unusual and is becoming a factor in facilitating M&A transactions in Japan because activist funds often demand divestment of non-core businesses.

The financial environment in Japan is also supportive of M&A activities regardless of whether the transaction is outbound or domestic. The Bank of Japan has implemented a number of monetary easing policies and the current interest rates on Japanese government bonds are close to zero. Japanese companies can benefit from the close-to-zero interest rates to finance their outbound M&A transactions. With the recent regulatory reforms allowing the carry-forward of capital gains tax in the context of share-for-share tender offer transactions, Japanese listed companies, which are said to hold more than US\$200 billion of treasury shares, will have another viable option to finance their acquisitions.

In addition, government-owned financial institutions such as the Development Bank of Japan and the Bank for International Cooperation are ready to provide additional financing support.

Also, the Innovation Network Corporation of Japan is continuing equity investments in various Japanese companies or in foreign companies jointly with Japanese companies.

We are therefore quite optimistic about the long-term future of the Japanese M&A market.

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