Shareholders' agreement and bye-laws Q&A: Japan

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This Q&A provides country-specific commentary on *Practice note, Shareholders' agreement and bye-laws: Cross-border*, and forms part of *Cross-border joint ventures*.

Shareholders' agreement and bye-laws

1. What are the main documents that regulate the constitutional arrangements and day-to-day operation of a joint venture company incorporated in your jurisdiction?

Articles of incorporation

This is the constitutional document of a joint stock corporation (*kabushiki kaisha*) (KK), which is the most commonly used vehicle for a private joint venture. The articles of incorporation (*teikan*) are prepared by the promoter (*hokkinin*) as the company's fundamental operational rules. The original articles typically include:

- Basic corporate information (for example, corporate name, business objective, location of principal office, method of public notice and fiscal year).
- Number of authorised shares.
- Number and type of shares to be issued.
- Amount of initial paid-in capital.
- Corporate governance matters, such as procedures for holding shareholders' meetings and board meetings, determining board composition and other management arrangements.

Super-majority voting provisions regarding certain corporate matters can also be included.

Shareholders' agreement

The shareholders of a joint venture commonly enter into a shareholders' agreement. While the terms of the articles of incorporation are, in general, strictly governed by the Companies Act, the shareholders can agree more flexible terms in the shareholders' agreement.

Typically, the shareholders' agreement contains the terms of the parties' agreement in greater detail, including:

- The number of board members to be designated by each shareholder.
- Any veto rights of the shareholders.
- The amount of initial contribution by each shareholder.
- Any additional financing commitment.
- Share transfer restrictions.

In a shareholders' agreement that is entered into on incorporation of the joint venture, the form of the articles to be used by the promoters is typically attached to the shareholders' agreement.

> 2. Is it possible to amend the constitutional documents of a company? If so, what are the relevant voting requirements? Can the shareholders amend the relevant voting majorities and, if yes, to what extent?

The articles of incorporation can be amended by a special resolution of the shareholders. This requires approval by two-thirds of the voting rights held by the shareholders present at a meeting, unless otherwise increased by the articles of incorporation. A special resolution is only valid if shareholders holding a majority of the company's voting rights (including those not present at the meeting) participate in the vote.

It is possible for shareholders to amend the constitutional documents to increase the relevant voting majorities required for various corporate actions (including the majority required to amend the articles), but articles cannot be amended to decrease the voting majorities below the minimum level required by law, which is either a simple majority or two-thirds, depending on the nature of the corporate action.

> 3. Is every shareholder automatically bound by a company's constitutional documents?

The articles of incorporation provide the fundamental rules to operate the company and are binding on the shareholders.

4. Is it necessary for a company's constitutional documents to be registered and open to public inspection?

The articles of incorporation of a private joint venture company are not registered for public inspection.

However, the commercial register of the company, which is publicly available, includes some items contained in the articles, such as:

- Corporate name.
- Corporate objectives.
- Principal address.
- Date of incorporation.
- Method of public notice.
- Number of authorised shares and shares issued by the company.
- Terms of class shares issued by the company.
- Outstanding stock acquisition rights issued by the company.
- Names of directors and statutory auditors.
- The name and address of representative director(s).

5. Is it necessary for a shareholders' agreement to be registered and open to public inspection?

No. The shareholders' agreement is not registered for public inspection.

6. Is a company bound by its constitutional documents?

Yes. A company is required to abide by its articles of incorporation.

7. Is it common practice for a joint venture company to be a party to a shareholders' agreement relating to the joint venture?

When establishing a new joint venture company, it is not common for that company to be a party to the shareholders' agreement. However, it can be a party if the shareholders want to directly bind the company in relation to specific obligations set out in the shareholders' agreement. For example, the shareholders might require the company to periodically submit its business plans to them, or contractually bind the company to accept certain audit rights of the shareholders.

8. What are the remedies for breach of a shareholders' agreement?

The non-breaching party can request specific performance and/or claim monetary damages.

9. What are the remedies for breach of a company's constitutional documents?

Breach of the articles of incorporation typically constitutes a breach of duty of care of a good manager by the directors of the company. In such an event, the shareholders can usually take action against the directors, possibly through a derivative suit or injunction.

10. In which document would you commonly insert the following provisions:

- (a) Object and scope of the venture.

- (b) Capitalisation and funding.
- (c) Board composition and management arrangements.
- (d) Distribution of profits (including dividend policy).
- (e) Provisions for dealing with deadlock.
- (f) Termination provisions.
- (g) Restrictive covenants.
- (h) Rights to appoint and remove directors.
- (i) Quorum for board and shareholder meetings.
- (j) Procedures for shareholders' meetings.
- (k) Division of shares into classes.
- (l) Chair's casting vote.
- (m) Notice provisions.
- (n) Share transfer provisions (including pre-emption rights).
- (o) Minority protection (veto rights, tag along rights and so on).
- (p) Drag along rights.

(a) Object and scope of the venture.

Articles of incorporation and shareholders' agreement.

(b) Capitalisation and funding.

The articles include the amount (or minimum amount) of assets to be contributed on incorporation, but do not contain the details of any additional financing commitments of each shareholder. Those details are commonly provided in the shareholders' agreement.

(c) Board composition and management arrangements.

The articles of incorporation usually set out the procedures for shareholders' meetings and board meetings, such as the requirements for validly convening the meeting, quorum and voting requirements, as well as the minimum and/or maximum number of directors or statutory auditors.

The shareholders' agreement would, in addition to what is provided in the articles, typically contain the number of directors and statutory auditors, if any, to be designated by each shareholder, or any other details regarding the management of the joint venture.

(d) Distribution of profits (including dividend policy).

Shareholders' agreement.

(e) Provisions for dealing with deadlock.

Shareholders' agreement.

(f) Termination provisions.

Shareholders' agreement.

(g) Restrictive covenants.

Shareholders' agreement.

(h) Rights to appoint and remove directors.

Shareholders' agreement.

(i) Quorum for board and shareholder meetings.

Articles of incorporation and shareholders' agreement.

(j) Procedures for shareholders' meetings.

Articles of incorporation and shareholders' agreement.

(k) Division of shares into classes.

Articles of incorporation and shareholders' agreement.

(l) Chairman's casting vote.

No casting vote can be granted to the chairman.

(m) Notice provisions.

Shareholders' agreement.

(n) Share transfer provisions (including pre-emption rights).

The articles of incorporation of a private joint venture company typically provide that share transfers are subject to approval by the board of directors (or by the shareholders' meeting, if the company does not have a board, see *Country Q&A, Joint venture structures: Japan: Question 9*).

The shareholders' agreement commonly provides that shares cannot be transferred without the prior written consent of the other shareholders. As an exception to this share transfer restriction, the shareholders' agreement frequently sets out certain right of first refusal or right of first offer mechanisms under which the shareholders wishing to

sell their shares will be permitted to do so after the non-transferring shareholders are given a prior opportunity to acquire such shares.

(o) Minority protection (veto rights, tag along rights and so on).

Shareholders' agreement. In addition, veto rights must be provided in the articles of incorporation if arranged as class shares with veto rights. In relation to certain corporate matters, super-majority voting provisions can also be provided in the articles.

(p) Drag along rights.

Shareholders' agreement.

11. In the event of a conflict between a shareholders' agreement and a company's constitutional documents, which document is likely to prevail?

Under Japanese law, the articles of incorporation prevail over the corporate actions of the company.

12. Which conditions are commonly inserted in a shareholders' agreement?

The conditions to be included would depend on the nature of the transaction, but perhaps most commonly *Standard document, Joint venture shareholders' agreement: majority and minority shareholder: Cross-border: clause 4.1(a)* and *clause 4.1(f)* would be included as a minimum requirement.

13. Is there any restriction under local law on the method that the joint venture partners may use to finance the joint venture?

There are no specific Japanese law restrictions with respect to the financing of a joint venture. Shareholders agreements for joint ventures typically provide that the joint venture is to obtain its own financing with no obligation on the joint venture partners to provide additional funding.

14. What are the consequences under local law for provisions in the shareholders' agreement and/or in a company's constitutional documents that are in breach of company law (for instance, are they void)?

Any provisions of a shareholders agreement that are inconsistent with the Companies Act would be unenforceable. Provisions of the articles of incorporation that are inconsistent with the Companies Act would be void.

15. Are the limitations set out in the objects clause in the constitutional documents of the joint venture enforceable against third parties (for instance, if the company enters into a transaction outside the scope of its objects clause, could the relevant transaction be set aside on the basis that the company acted ultra vires)?

Technically, transactions outside of the scope of a company's objects as set out in its articles of incorporation would be void. However, in practice the scope of objects would commonly include activities that are ancillary or necessary to achieve the specific activities prescribed in the articles and hence would be interpreted broadly. Therefore, not many transactions would be likely to fall outside the scope of the objects.

16. Is the shareholders' liability limited to the amount of their respective equity contributions to the joint venture?

Yes, except in extraordinary cases where the "piercing the corporate veil" doctrine might apply. This doctrine could apply in cases where the legal personality is either abused to avoid the application of laws or has no substance.

17. Are there any statutory requirements applicable to the directors' authority and powers, such as to their ability to delegate to committees or individual directors?

A director cannot attend board meetings by proxy and must cast their own vote. The board may by its resolution delegate certain matters to committees or individual directors.

18. Are there any statutory requirements applicable to the board of directors' meeting, such as:

- (a) The country in which they should be held.
- (b) The procedure to call and adjourn a meeting.
- (c) The procedure to participate to and vote in a meeting.
- (d) Who should chair a meeting.
- (e) The role, if any, of the Company secretary.
- (f) How the board decisions should be recorded.

(a) The country in which they should be held.

There is no specific rule on location, but directors must be given a reasonable opportunity to attend meetings.

(b) The procedure to call and adjourn a meeting.

When convening the board meeting, a notice must be sent to all directors at least one week before the day of the meeting, unless a shorter notice period is provided by the articles of incorporation. If the consent of all directors is obtained, a board meeting may be held without complying with the notice requirements.

(c) The procedure to participate to and vote in a meeting.

No proxy is permissible, but attendance can be by video or telephone conference if discussions can be held in a form comparable to an in-person meeting.

(d) Who should chair a meeting.

There is no specific rule under law, but in most cases the chair is appointed in the articles.

(e) The role, if any, of the Company secretary.

The Companies Act does not provide for a company secretary position.

(f) How the board decisions should be recorded.

Companies are required to document board decisions in board minutes and to keep the minutes at the principal office for ten years.

19. Are there any statutory provisions regulating directors' conflicts of interest?

If a director has a "special interest" in resolutions to be passed by the board of directors, the director cannot participate in the resolution. For instance, where a director carries out transactions in competition with the company, or where a conflict of interest occurs between the director and the company, the director must abstain from the voting and also refrain from participating in the discussions for the resolution. In addition, the transaction must be approved by a board resolution.

The examples of conflict of interest transactions include the purchase of the company's products or other assets by a director, sale of a director's own products or other assets to the company and loans from the company to a director. In addition, indirect conflict of interest transactions, such as the guarantee of a director's obligations granted by the company, are also subject to board approval. Once the board has approved the transaction, the director must report material facts concerning such transaction, such as a summary of the transaction, to the board of directors without delay.

Further, if a director intends to engage in any activities that fall "in the line of business of the company", the director must obtain the approval of the board of directors to carry out the competing transaction. On approval of the board of directors, the director must report material facts concerning such transaction, such as a summary of the transaction, to the board of directors without delay after the director has implemented the competing transaction.

20. Are there any statutory requirements in relation to the directors' remuneration?

Unless the amount of directors' remuneration is provided in the company's articles, it must be determined at a shareholders' meeting. A shareholders' resolution or the company's articles may provide the maximum amount of total remuneration for all directors. The allocation of total remuneration to each director may be delegated to be determined by the board of directors. In practice, many companies set a remuneration formula based on the position of each director.

21. Are there any statutory requirements applicable to the appointment and removal of the directors? Can alternate directors or board observers be appointed?

Directors are appointed by an ordinary resolution at the shareholders' meeting. A substitute director may be appointed in preparation for cases where there is a vacancy resulting in a shortfall in the number of directors prescribed in laws and regulations or the articles of incorporation.

Directors may be dismissed at any time by an ordinary resolution at the shareholders' meeting (that is, by a majority of the voting rights held by the shareholders present at a meeting). The Companies Act permits companies to increase such resolution requirement in the articles of incorporation. If a director is dismissed at a shareholders' meeting before the expiration of their term of office, without a justifiable ground, such director may demand damages arising from the dismissal.

22. What is the procedure to be validly recognised as a shareholder? Are share certificates issued and, if they are, what is the procedure to replace them?

Share certificates will be issued only if the articles of the company provide that it will issue share certificates for its shares (which has recently become uncommon). Shareholders who have lost their share certificates may make a request to the company to register such loss of the share certificates, in which case the company will state or record such loss in the registry of lost share certificates. A share certificate in the registry of lost share certificates will become invalid after one year has elapsed from the day immediately following the day of such registration, in which case the registrant may obtain a reissued share certificate from the company. The shareholder will retain its rights, such as the right to vote and to receive dividends, during this period if it is registered in the company's shareholder registry.

In companies that do not issue share certificates, ownership of shares must be stated or recorded in the shareholder registry of the company.

With respect to a share transfer, if the company issues share certificates, a transferee of such share transfer shall be validly recognised as a shareholder by the company by presenting the share certificate and requesting the company to update the shareholders’ register. If the company does not issue share certificates, in general, a transferee of a share transfer shall be validly recognised as a shareholder by the company by presenting a request form, signed or sealed by the transferor and transferee, directing the company to register the transferee as the holder of the shares on the shareholder registry of the company.

23. Are there any statutory provisions governing the declaration and payment of dividends and other distributions? Is it possible for a shareholder to waive its right to receive a dividend?

In general, an ordinary resolution at the shareholders' meeting is required to distribute dividends of surplus. Under certain circumstances, dividends of surplus may be determined by the board of directors, if so prescribed in the company's articles. There are certain financial restrictions on distributing dividends of surplus. The total book value of money and other property to be distributed to the shareholders must not exceed the "distributable amount" as of the day of the distribution.

A shareholder may elect not to receive dividends. In addition, the company's articles would often provide that the company will be exempted from the obligation to pay dividends if such dividends remain unclaimed for a certain number of years.

24. Are there any statutory requirements applicable to the shareholders' meeting, such as:

- (a) The country in which they should be held.
- (b) The procedure to call and adjourn a meeting.
- (c) The procedure to participate (in person or by proxy) to and vote in a meeting.
- (d) Who should chair a meeting.
- (e) The role, if any, of the Company secretary.
- (f) How the shareholders' resolutions should be recorded and amended.

(a) The country in which they should be held.

There is no rule as to the country in which a shareholders meeting should be held, but if it is held at a place that makes it difficult for shareholders to attend, then the resolutions made at such shareholders meeting could be revoked.

(b) The procedure to call and adjourn a meeting.

A notice to convene a shareholders' meeting of a private company must be dispatched to shareholders one week before the date of the proposed shareholders' meeting. A resolution on adjournment of the meeting may be passed by ordinary resolution to continue the proceedings at a later date.

(c) The procedure to participate (in person or by proxy) to and vote in a meeting

Shareholders may exercise their votes by proxy. In practice, the articles of incorporation often limit the right to grant proxies only to shareholders of the company.

(d) Who should chair a meeting.

The chairperson will be appointed at the shareholders' meeting, if the identity of the chairperson is not determined in the articles of the company. The articles of many companies provide that the president of the company will act as the chair of the shareholders' meetings.

(e) The role, if any, of the Company secretary.

The Companies Act does not provide any secretary system.

(f) How the shareholders' resolutions should be recorded and amended.

Minutes of the shareholders meeting must be prepared. A resolution can only be amended by another shareholder resolution.

25. Are company seals required?

At least one representative director must record their corporate seal with the local legal affairs bureau (*houmukyoku*).

26. Are there any restrictions under local law to include indemnity provisions for the benefit of the directors or officers of the company in the company's constitutional documents?

Indemnity provisions are not common in Japan. Instead, certain limitations of liability are often provided in the articles. Specifically, liability of directors other than outside directors (except a representative director) may be limited under certain circumstances to a maximum of their remuneration for four years. With regard to the representative director, such limitation is set at a maximum of their remuneration for six years. A further limitation applies to outside directors, at a maximum of their remuneration for two years. In addition, the company may, under the provisions of its articles, enter into an agreement with any directors other than executive directors to determine their maximum amount of liability in advance.

27. In relation to cross-border joint ventures that present a connection to the UK, have you noticed the introduction of any "Brexit" wording in the shareholders' agreement or other joint venture document?

We have not noticed the introduction of any “Brexit” wording.

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