3. Commercial Law

1. An Act to Partially Amend the Commercial Code and Related Laws

Law No. 71. Promulgated on June 6. 1997. Effective as of October 1, 1997.

[Background of the Legislation]

The provisions for procedures of merger or consolidation in our Stock Corporation Law are influenced by Italian Law, German Law, American Law and the like, as well as our own laws. In our Stock Corporation Law, there are also provisions applying to procedures for merger or consolidation, which were originally provided for in other procedures. Furthermore these provisions were enacted or revised at different times, therefore, regulation of mergers or consolidations lacked consistency. There was also a shortage of provisions which seemed to be necessary. If there were any procedures, they were insufficient, while highly complex procedures were required.

Under these conditions, for a long time it has been thought necessary to completely reexamine the provisions for mergers or consolidation, to attempt to simplify and rationalize the requirements for excessively complicated proceedings, and to enrich and clarify the insufficient provisions.

In 1975, "Problems concerning the Amendment of the Stock Corporation Law" was published by the Counselor's Office of the Civil Affairs Bureau of the Minister of as a step to completely and fundamentally amend our Stock Corporation Law, which partially encompasses procedures for mergers or consolidation. After the enactment of the new amendment concerning Stocks, Organs, Accounting and Disclosure Systems for Stock Corporations in 1981, to address the problems left unsolved in that Amendment, "Problems concerning Merger and Consolidation, and Legislation for Separately Regulating Large and Small (Publicly and Closely Held) Corporations" was published

by the Counselor's Office in 1984, and opinions about it were solicited. Referring to opinions submitted, in 1986 the "Draft Amendment of the Commercial Code and the Law of Limited Liability Companies" was published by the Counselor's Office.

Some of the issues roused in that draft were incorporated in the 1991 Amendment, but the amendment concerning merger and consolidation procedures was shelved. Thereafter, the draft amendment provisions were prepared for the 1993 and 1994 amendments of the Commercial Code. The Commercial Code Division of the Legislative Council of the Ministry of Justice, an advisory organ to the Minister for Justice, decided on March 1995 that procedures for merger and consolidation and procedures for the division of corporation should be given consideration for the next amendment of Commercial Code. But the Commercial Code Division began to deliberate the former apart from the latter, since financial circles required early amendment of the former in 1996. As the result, on January 22, 1997, the Commercial Code Division formulated a proposal for the principles of a bill, and that proposal was approved at a general meeting of the Legislative Council of the Ministry of Justice on February 14. For the most part, these principles follow along the lines of the 1980 draft, and provided more detail than the earlier draft. In response to these principles, on March 7, 1997, an "Act to Partially Amend the Commercial Code" was introduced to the Plenary Session of the Diet, and approved on May 30.

[Main Provisions of the Act]

(1) Simplification and improvement for merger and consolidation.

First, the general meeting report on matters relative to the merger after the procedure for merger has been completed in the case of merger, and the inaugural general meeting in the case of consolidation were abolished. The reason is that under old law of either merger or consolidation, a general meeting to approve a written agreement for merger or consolidation also had to be held, but this required two general meetings which was thought to be unreasonable. The abolition of this requirement will bring about a shortened timeframe and cost saving in the procedures for merger or consolidation. With this abolition,

the activities performed in merger or consolidation will be performed by a general meeting to approve a written agreement. Therefore, the new law provides that the agreement for merger or consolidation shall state, in the case of a merger, such amendments or changes in certificate of incorporation of the surviving corporation as are desired to be effectuated by the merger (Article 409(1)), and in the case of a consolidation, provision of the certificate of incorporation of the resulting corporation (Article 410(1)). Furthermore, certain statements that should be attached to the notice to each shareholder in case of merger or consolidation, shall be open to examination by any shareholder or creditor for six months after the date of registration of the merger or consolidation (Article 414-2).

Secondly, the proceedings for the protection of creditors were improved. The individual notice to any creditor known to the corporation requesting him/her to produce a claim may be omitted in the instance when the articles of incorporation provide that public notice for merger or consolidation shall be given by having it published not in the Official Gazette but in a daily newspaper carrying current events, and the corporation actually gives such public notice by having it published in both (Articles 100, 412). Furthermore, under old law, if any creditor produced a claim, a corporation had to discharge his/her liabilities, provide him/her with appropriate security, or entrust appropriate property to a trust company (Articles 100(3), 416(1)). Under the new law, however, a corporation need not take such measures for any creditor who would not be prejudiced by merger or consolidation (Article 100(3) *proviso*).

Thirdly, the procedures for so-called small scale mergers have been newly established. Under such procedures, a surviving corporation need not hold a general meeting when the total number of new shares to be issued at merger dose not exceed one-twentieth of the total number of outstanding shares in such corporation, and an amount payable to the shareholders of the terminated corporation dose not exceed one-fiftieth of the net assets of the surviving corporation (Article 413.3(1)). This procedure may not be utilized in cases when the total number of shareholders including dissenting shareholders exceeds one-sixth of the total number of outstanding shares in the surviving corporation (Article

413.3(8)). Using this procedure, the constituent corporation shall state in its written agreement for corporate merger that it will not hold a general meeting (Article 413.3(3)), and the surviving corporation shall, within two weeks of the day of preparing the written agreement for merger, give public notice or notice to each shareholder of the new business name, the address of the head office of the terminated corporation, the time when the merger is to be effected, and omission of the general meeting (Article 413.3(4)). A dissenting shareholder shall, within two weeks of the date of such public notice or notice, notify the corporation in writing of his/her objection to the proposed merger in order to exercise his/her appraisal right (Article 413.3(5)).

(2) Enrichment of The Disclosure System.

Under the old law, a constituent corporation was required to have in the calling notice for general meeting to each shareholders the substance of the written agreement for merger or consolidation, and to deposit at the head office only the balance sheet of the corporation before the general meeting. Under new law, the statement to be deposited beforehand must included: ① the written agreement; ② a statement prescribing the reason for the ratio of allotment of new shares to the shareholders of the terminated corporation; ③ the balance sheet of each corporation prepared within six months of the date of the general meeting held to approve the written agreement for merger or consolidation; ④ if such balance sheet is not of final one, then a final one must be provided; ⑤ the statement of profits and losses prepared simultaneously with the final balance sheet; ⑥ if the statement of profits and losses is prepared simultaneously with the balance sheet described in item 3 above, such a statement must also be provided (Article 408.2(1)).

(3) Other Provisions.

Under this Amendment, it becomes permissible for a stock corporation to be formed as a result of the consolidation of two limited liability companies, and a limited liability company may be formed as a result of the consolidation of two stock corporation (Articles of the Limited Liability Company Law 59, 60).

2. An Act to Partially Amend the Commercial Code

Law No. 56. Promulgated on May 21, 1997. For transferring a corporation's own shares, effective as of June 1, 1997. For the giving of pre-emptive rights, effective as of October 1, 1997.

[Background of the Legislation]

There are two ways in which a corporation transfers to a rightful claimant its own shares when he/she exercises a right to stock options. The first is that a corporation gives him/her its own shares acquired by itself in advance, and the second is that a corporation gives him/her pre-emptive right to subscribe to new shares at a certain price. Under the old law, a corporation could not acquire its own shares to transfer to its directors, and its own shares acquired to transfer to employees had to be transferred within six month after the date of acquisition. Furthermore, a resolution in the general meeting to approve the issuance of new shares to parsons other than shareholders at an especially favorable price had to be in effect for one-time issuing new shares which would be paid in within six months after the date of such resolution (Article 280.2(2), (4)). Due to these points, it is almost impossible for a corporation to directly put into operation a stock option plan which is a long-term reward plan. Therefore, some publicly held corporation have put into operation pseudo stock option plans using the pre-emptive right of debenture with pre-emptive right which may be assigned in isolation.

Under these circumstances, since February 1997, the Law Division of the Liberal-Democratic Party has been discussing about providing procedures for stock option plans applicable to any stock corporation. As a result, it drafted "the Bill of an Act to Partially Amend the Commercial Code". This bill was introduced to the Plenary Session of the Diet by its members on April 1997, and approved on May 16. The reason for introducing this bill is to motivate directors and employees, thereby improving results and increasing competitiveness of businesses, by providing procedures for creation of a stock option plan. Under the new law, a corporation may either transfer its own share or give pre-emptive rights for a stock option plan.

[Main Provisions of the Act]

(1) Transferring a Corporation's Own Shares for a Stock Option Plan

Under the new law, a corporation may acquire its own shares to transfer not only to its employees but also to its directors (Article 210.2(2)③). The total number of its own shares that a corporation may acquire to transfer to its directors and employees for the purpose of giving them stock options, added to those used for other purposes, increases to one-tenth of the total number of its outstanding shares (Article 210.2(1)(3)). If a corporation acquires shares for the purpose of giving stock options, then the adoption of a resolution at a general meeting is required which must give the names of directors and employees to be given stock options, class, number and price of shares to be transferred to them, the period of time in which the stock option right may be exercised, and the terms for its exercise (Article 210.2(2)①). A corporation shall fix as the period of time in which the stock option right may be exercised a period within ten years from the date of the resolution of such general meeting (Article 210.2(4)). The class, number, and total transfer-price of its own shares acquired by a corporation to be transferred its directors or employees based on the agreement to provide a stock option shall be also approved by the majority at the same general meeting (Article 210.2(1)①). If a corporation acquires its own shares based on the resolution of such general meeting, it shall acquire those by the completion of the first regular general meeting held after such resolution (Article 210.2(6)). The acquisition price of such shares of the corporation may not exceed the amount of profits available for dividends (Article 210.2(3)). A listed corporation shall acquire its own shares through the stock exchange. A corporation whose securities are traded over-the-counter may acquire its own shares through such market. A listed corporation may acquire its own shares by means of a tender offer (Article 210.2(10)). A corporation whose securities do not have public marketability shall acquire its own shares by means of face-to-face transactions with its shareholders. In that case, matters concerning acquisition of the corporations own shares, including the name of any transferor, shall be ap-

proved by resolution of the general meeting provided for by Article 343 (Article 210.2(2)②, (7)).

(2) Giving Pre-emptive Right for a Stock Option Plan

To give stock options to directors or employees through the granting of a pre-emptive right, a corporation shall set forth in its articles of incorporation the provision therefor (Article 280.19(1)). Furthermore, such a resolution, as provided for in Article 343, is required to give be names of directors and employees to be given pre-emptive rights, the class, number, issue price of the shares constituting the object of such pre-emptive rights, whether such shares have par value or not, the period of time during which the stock option right may be exercised, and the terms for its exercise (Article 280.19(2), (7)). The total number of shares constituting the object of pre-emptive rights to be given by such resolution and the number of shares constituting the object of pre-emptive rights which had been formerly given by the same article except for yet issued shares, may not exceed one-tenth of the total number of outstanding shares (Article 280.19(3)). A corporation shall fix as the period of time in which right of stock option may be exercised the period within ten years after the day of the resolution of such general meeting (Article 280.19(4)). A corporation shall give such pre-emptive rights within one year after the date of that resolution (Article 280.19(6)). Such pre-emptive rights may not be transferred (Article 280.20).

3. An Act Regarding Exceptional Rules of the Commercial Code Concerning the Procedures for Retirement of Shares

[Background of the Legislation]

The 1994 Reform Act permits a corporation retirement of shares with the profits available for distribution to the shareholders based on the resolution at a regular general meeting (Article of the Commercial Code 212.2). Under this procedure, a general meeting is required each time there is retirement of shares. That is one of the reasons why the number of corporations which have published a plan for retirement of shares is only twenty-three. Under these circumstances, since February

1997, the Law Division of the Liberal-Democratic Party began to deliberate on the relaxation of the procedures. As a result, it drafted "the Bill of an Act Regarding Exception Rules of the Commercial Code Concerning the Procedures for Retirement of shares". This bill was introduced to the Plenary Session of the Diet by its members on April 1997, and approved on May 16. The reason for the introduction of this bill is to promote the efficiency and activity of the capital market by relaxation of the procedures for retirement of shares.

[Main Provisions of the Act]

Under this Act, a listed corporation or a corporation whose securities are traded on the over-the-counter market may acquire and retire its own shares based on the resolution of the directors meeting, if it shall be specially deemed to be necessary considering the corporation's affairs, property, and other conditions. In this case, the corporation shall set forth provisions thereof in its articles of incorporation (Article 3(1)). Furthermore, the corporation shall set forth in its articles a provision concerning the number of shares to be acquired and retired (Article 3(2)), and such number may not exceed one-tenth of the total number of its outstanding shares (Article 3(3)). If a corporation acquires and retires its own shares based on the resolution of the directors meeting, it shall acquire those by the completion of the first regular general meeting to be held after such resolution (Article 3(6)). The total acquisition price of such shares may not exceed one half of the amount obtainable by deducting the amount that had actually been granted as an interim dividend from the amount available for the interim dividend (Article 3(5)).

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