

Review of the tender offer rule & the large shareholding reporting rule



金融庁

Financial Services Agency, the Japanese Government

September 2023

I. Introduction

II. Tender Offer Rule

III. Large Shareholding Reporting Rule

IV. Transparency of Beneficial Shareholders

Introduction

- ❑ At a joint session of the general meeting of Financial System Council and the meeting of Sectional Committee held in March 2023, the following consultation was delivered: **in light of securing transparency and fairness of the market and promoting constructive dialogue between companies and investors, the tender offer rule and the large shareholding reporting rule should be reviewed.**
- ❑ **A working group was established** to consider the following main issues based on recent changes in circumstances on **June 5, 2023.**

Recent Changes in Circumstances

Main Issues

Tender offer rule

- Increase in cases of unsolicited M&A through on-market transactions
- Diversification of M&A

- **Review of the scope of application of the tender offer rule (market trades, thresholds)**
- **Measures against coercive tender offers**
- Flexibility in tender offer rule

Large shareholding reporting rule

- Increase in passive investment
- Expansion of collaborative engagement
- Growing importance of constructive dialogues between companies and investors

- **Clarification of eligibility to use special reporting**
- **Clarification of the scope of joint holders**
- Clarification of treatment of cash-settled equity derivatives

Beneficial shareholders transparency

- **Measures to ensure transparency of beneficial shareholders**

I. Introduction

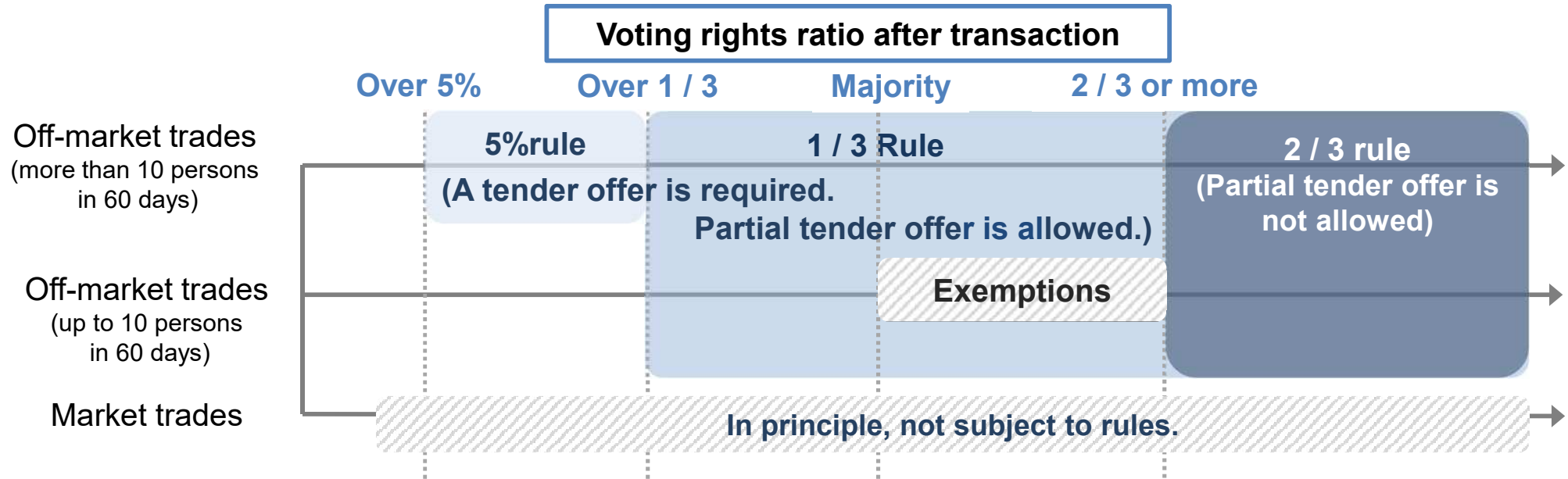
II. Tender Offer Rule

III. Large Shareholding Reporting Rule

IV. Transparency of Beneficial Shareholders

Overview of the Tender Offer Rule

- The tender offer rule forces a tender offer for the following transactions, and requires (i) prior information disclosure and (ii) equal treatment of shareholders in order to ensure the "transparency and fairness" of securities transactions that may have an impact on corporate control.



- The main regulations on the implementation of a tender offer are as follows:

Disclosure regulations

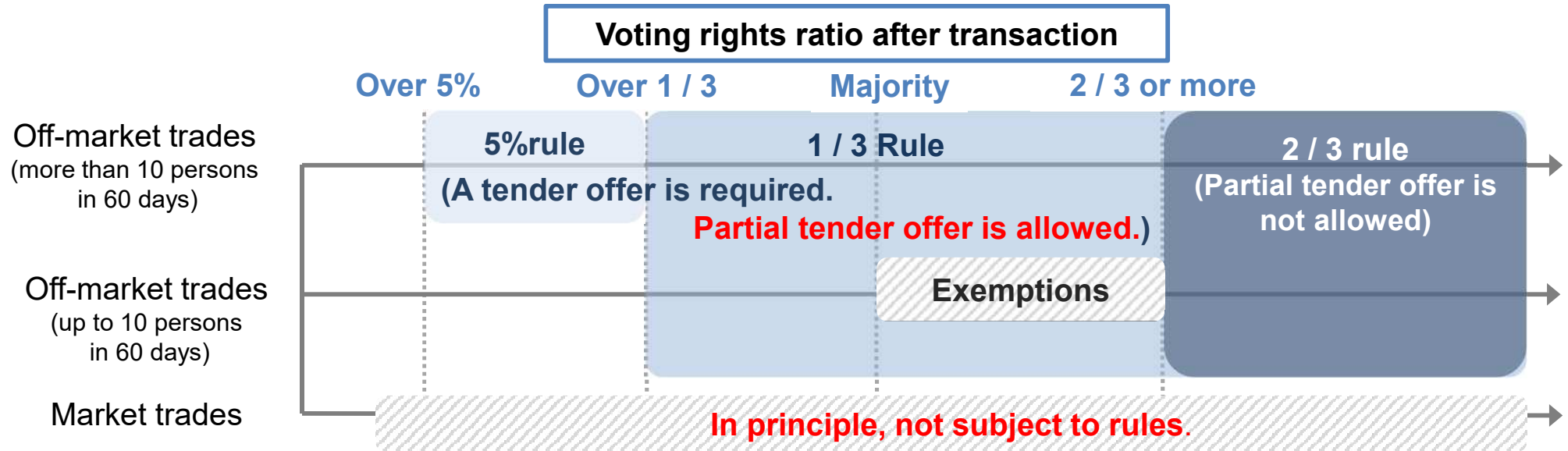
- ✓ The offeror must disclose the volume to be purchased, the tender offer price and tender offer period in advance.
- ✓ The target company must disclose the opinion with respect to the tender offer.

Other regulations

- ✓ A minimum tender offer period of 20 business days (a maximum of 60 business days) must be set.
- ✓ The tender offer price shall be the same for all shareholders.
- ✓ During the tender offer period, the offeror must not purchase shares other than through a tender offer.
- ✓ The offeror must not change the terms and conditions to the disadvantage of shareholders.

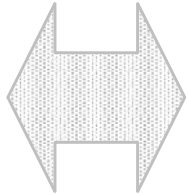
Main issues to consider

- It has been pointed out that (i) **transactions in which more than 1 / 3 of the voting rights are acquired through market trades should also be subject to tender offer rule** and (ii) **the scope of the partial tender offer should be limited** because the partial tender offer could be coercive.



Japan 

- ✓ Transactions in **which more than 1 / 3** of the voting rights are **acquired through market trades** are **not subject to** tender offer rule.
- ✓ **Partial tender offer** is **allowed** if the **ratio of voting rights** after the tender offer is **less than 2 / 3**.



Europe  

- ✓ **Regardless of the type of transaction**, a **tender offer** is **required** when a **certain threshold** is exceeded.
- ✓ In principle, **partial tender offer** is **not allowed**.

Main issue (1): Market trades

- ❑ It has been pointed out that market trades should be subject to the tender offer rule (1/3 rule).

Comments on the Current Rule

- ❑ The current tender offer rule does not apply to a market trade unless it falls under so-called “rapid accumulation,” given that a certain degree of transparency and fairness is ensured.
- ❑ On the other hand, recently, there have been cases of acquiring more than 1/3 of the voting rights through market trades. In such transactions, it has been pointed out that general shareholders are not given sufficient information or time necessary for investment decisions and that there are issues of coercion (see the decision of the Tokyo High Court below). Therefore, it has been pointed out that market trades should be subject to the tender offer rule (1/3 rule).

Tokyo High Court, decision of November 9, 2021

“The appellants purchased shares whose ownership ratio of share certificates exceeds 1/3 in a short period of time through acquisition of shares on market trades that is not subject to the tender offer rule. Such purchase does not provide general shareholders with sufficient information and time necessary for investment decisions and tends to make general shareholders take actions to avoid such risks if they think that the corporate value of the company may be damaged by the acquisition of control by the purchaser. Therefore, such purchase is recognized to have an incentive to sell or pressure to sell (coercion) for general shareholders.”

Issues to be discussed

- ◆ What is your view on **making transactions for acquiring more than 1/3 of the voting rights through market trades subject to the tender offer rule?**

Main issue (2): Measures against Coercive Tender Offer

- ❑ It has been pointed out that certain measures should be taken against a coercive tender offer.

Comments on the Current Rule

- ❑ In the case of a tender offer that is expected to reduce the corporate value of the target company after the acquisition of control, there is a problem in that general shareholders have an incentive to apply for the tender offer in order to avoid disadvantages due to the reduction in corporate value (so-called coercive tender offer). There is a risk that general shareholders may be forced to accept the tender offer price at an unreasonably low price, and that acquisitions that reduce corporate value will tend to be more successful. It has also been pointed out that these risks are more likely to occur in a partial tender offer (tender offer with an upper limit) than in a tender offer without an upper limit. (Note).
- ❑ In order to address the issue of the coercive tender offer, the following measures could be taken with reference to the Takeover Code in the UK.

Measures to eliminate or reduce the risk of coercion

- I A measure to lower the threshold (currently 2/3) at which a partial offer is allowed.
- II A measure that requires an additional tender offer period after the tender offer is successful.
- III A measure that allows the implementation of the partial tender offer only when shareholders with a majority of the voting rights approve it.

Issues to be discussed

- ◆ What is your view on the **implementation of measures to address the issue of coercive tender offer and the content of such specific measures?**

(Note) In the case of a tender offer without an upper limit, since the tender offeror must purchase all the tendered shares, in order to make it economically viable for the tender offeror, the tender offer price must be set lower (compared to the case of a partial tender offer), and it has been pointed out that it is likely to be possible for each shareholder to choose not to tender predicting that other shareholders will also not subscribe.

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Overview of the large shareholding reporting rule

- ❑ The large shareholding reporting rule requires large shareholders to disclose the status of shareholdings in order to improve the transparency and fairness of the market by promptly providing the information.
- ❑ This rule is divided into “**general reporting**,” which is a basic disclosure type (cf. Regulation 13D in US), and “**special reporting**,” which allows special measures for institutional investors (cf. Regulation 13G in US).

General Reporting

Obligations of Large Shareholders

1. If an investor becomes a large shareholder (**more than a 5% stake**):
 - The investor must **submit a large shareholding report within five business days** of acquiring more than a 5% in a company.
2. If there are any significant changes, such as **a 1% or greater increase/decrease** in the percentage of shareholdings following the submission of the large shareholding report:
 - The investor must **submit a “change report” within five business days of the change**.

Special Reporting

Outline of the Special Reporting Rule

The rule allows institutional investors who repeatedly and continuously execute buy/sell transactions of shares in their daily operations to report under relaxed frequency of submissions.

<Details of the relaxation>

Only **to submit a “large shareholding report” and “change report” within five business days of the pre-registered reference date set twice a month**.

<Eligibility to use special reporting>

1. The investor’s ownership ratio does not exceed 10%.
2. **The investor is not committing to the Act of Material Proposal.**
3. It is necessary to register the reference date to the authority.

Joint Holders

Treatment of Joint Holders

A shareholder is required to calculate its shareholding ratio by including the shareholding of a person that corresponds to any one of the following (“Joint Holder”).

1. A person that **has agreed to obtain or assign shares in cooperation with the shareholder**.
2. A person that **has agreed with the shareholder to jointly exercise voting rights** and other shareholder rights.
3. A person that has a special relationship with the shareholder, such as a certain capital relationship or a family relationship.

Main issues to consider

- ❑ From the viewpoint of promoting effective engagement with companies by investors, it has been pointed out that **the scope of "material proposal" should be limited or clarified**.
- ❑ It has been pointed out that **the scope of "joint holders" should be limited or clarified** from the viewpoint of promoting collective or collaborative engagement.

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Main issue (1): Scope of the Act of Material Proposal

- It has been pointed out that the scope of "the act of material proposal" is unclear so that it becomes an obstacle to effective engagement between companies and investors.

Comments on the Current Rule

- Under the large shareholding reporting rule, a special reporting rule has been established for institutional investors to ease the frequency of submission. However, in order to be eligible for the rule, it is necessary that the purpose of shareholding is not to engage in "the act of a material proposal" to investee companies.
- Although the interpretation of "the act of material proposal" was clarified when formulating the Stewardship Code, it has been pointed out that further clarification is necessary in order to promote effective engagement.

Guideline published in 2014

1	Request explanation of management policies.	May not be considered "Material Proposal"
2	Explanation for a specific plan for exercising voting rights	
3	Request for an explanation of the stance given on ②	
4	Ask questions at a general shareholders meeting	
5	Request for resolution of specific matters at a general shareholders meeting	May be considered "Material Proposal"
6	Request changes in business policies	

Issues to be discussed

- What is your view on **limiting or clarifying the scope of "the act of material proposal"** in order to promote effective dialogue between companies and investors?

Main issues to be addressed

This arrangement has become a certain interpretation guideline. However, the following points are raised.

- The subject of the material proposal is comprehensive and as **the proposal relates to capital policy or business strategy, it may be regarded as a material proposal.**
- Issues can only be communicated indirectly through inquiries with the company, and **proposals cannot be communicated directly, so the company cannot understand the intention.**

Main issue (2): Scope of the Joint Holders

- ❑ It has been pointed out that the scope of "joint holders" is so unclear that it becomes an obstacle to collective or collaborative engagement.

Comments on the Current Rule

- ❑ Under the large shareholding reporting rule, shareholders are required to calculate their shareholding ratio including the shareholdings of "joint holders."
- ❑ At the time of formulating the Stewardship Code, the interpretation of "joint holders" was clarified. However, in light of the recent increase in collective or collaborative engagements, it has been pointed out that the scope of "joint holders" needs to be further clarified.

Guideline published in 2014

In principle, the following cases may not be considered "joint holders":

- ✓ The agreement between an investor and another investor remains within the scope of shareholders' general activities that are unrelated to the exercise of legal rights.
- ✓ In the situation where an investor in discussions with another investor communicates their plan for the exercise of voting rights and finds that the plan is the same as the other investor.

Main issues to be addressed

This arrangement has become a certain interpretation guideline. However, the following points are pointed out.

- There is a concern that if an investor who participated in the collective or collaborative engagement submits a shareholder proposal, and then the other investor agrees to it, the other investor may be considered as a "joint holder";
- The concept of "joint exercise of voting rights" can be read as a very comprehensive regulation, with no limitations on the purpose of controlling management.

Issues to be discussed

- ◆ Given that it has been pointed out that the interpretation of "joint holder" is unclear when conducting collective or collaborative engagements, what is your view **on limiting or clarifying the scope of "joint holders"**?

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Transparency of beneficial shareholders

- It has been pointed out that **the transparency of beneficial shareholders should be improved with reference to systems in other countries** in order to promote dialogue between companies and investors.

(*)The term "**Beneficial shareholder**" here **means** a person who is not a shareholder on the shareholder register (nominee shareholder) but **who has the authority to give instructions on voting right and investment**.

Japan



- As for nominee shareholders, there is a system for companies and other shareholders to identify through shareholder register or disclosure of major shareholders in annual securities reports.
- On the other hand, as for beneficial shareholders, there is no system for companies or other shareholders to identify unless they are subject to the large shareholding reporting rule (more than 5%).

Systems in other countries

US



- An institutional investment manager that exercises investment discretion over \$100 million or more in securities that trade on a national securities exchange must report details of its holdings including the name of the issuer and class, the CUSIP number, the number of shares and the total market value quarterly on Form 13F with SEC. Form 13F filings are publicly disclosed on EDGAR database.

UK



- A public company may give notice to any person whom the company knows or has reasonable cause to believe to be interested in the company's shares with voting rights issued to confirm the fact.
- Those who received such notice are required to confirm whether or not it is the case, and if he or she holds or has held any such interest, to give further information including the information enough to identify persons interested in the shares in question and the number of shares within such reasonable time as may be specified in the notice.

Issues to be discussed

- What is your view on **the necessity and content of measures to enable the company and other shareholders to effectively identify beneficial shareholders?**

- ❑ ICGN Global Governance Principles establishes principle regarding transparency of beneficial shareholders as follows.

ICGN Global Governance Principles

Principle 9: Shareholder rights

9.6 Shareholder registration

The board should ensure that the company maintains a record of the registered owners of its shares or those holding voting rights over its shares.

Registered shareholders, or their agents, should provide the company (where anonymity rules do not preclude this) with the identity of beneficial owners or holders of voting rights when requested in a timely manner. Shareholders should be able to review this record of registered owners of shares or those holding voting rights over shares.

(Reference)

Principle 10: Shareholder meetings

10.11 Vote confirmation

Companies should confirm to shareholders (where the beneficial owner appears on the share register) whether their votes have been validly recorded and formally counted. This normally can only be provided where the institutional investors hold shares in their own names rather than through pooled or omnibus accounts which co-mingle the securities of multiple investors.

Companies should also be able to clarify the reasons why they may reject any votes that have been submitted.