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Conduct of an Initial Public Offering in Japan by Means of the Over-the-Counter Registration of Stock

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Conduct of an Initial Public Offering in Japan by Means of the Over-the-Counter Registration of Stock

Rexford Coleman*

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This article conforms with R. COLEMAN, STANDARD CITATION OF JAPANESE LEGAL MATERIALS (1963).
The normal way to conduct an initial public offering of the sale of shares of stock in Japan without a securities exchange listing is through an over-the-counter (OTC) registration with the Association Juridical Person: Japan Securities Business Association1 (called in English the “Japan Securities Dealers Association” and commonly referred to as “JASDA”).2 Therefore, all stock sold publicly within Japan other than that listed on a securities exchange or sold under the special rules applicable to foreign securities is designated as an “over-the-counter valuable security.”3

3. Regulations Concerning the Sale of Valuable Securities Over-the-Counter and Other Transactions 店頭における有価証券の売買その他の取引に関する規則, JASDA Fair Practice Regulation No. 1, established June 18, 1976 and as amended through March 25, 1998, art. 2 (i) [hereinafter cited as “Fair Prac. Reg. 1”]. An older English translation is contained in JASDA REGULATIONS 27 under the title “Fair Business Practice Regulation” although the word “Business” does not appear in the Japanese title. “Valuable security” (えきsha ken 有価証券) is a technical word of art in Japanese law, derived from the German term Wertpapier, which determines the sort of instruments that are subject to the Securities Exchange Law. Securities Exchange Law 証券取引法, Law No. 25 of 1948 and as amended through Law No. 120 of 1997,
This registered share system was established to provide access to Japanese capital for small and medium sized Japanese domestic companies unable to be listed on the second division of a securities exchange. The present structure of this market (there were earlier versions) was created in November 1983, founded principally on an October 1981 report of the Securities Investigation Mission of JASDA based on a study of the NASDAQ system in the United States.

This Japanese registered share system is not generally available for shares of stock in non-Japanese companies whose domestic sale in the Japanese over-the-counter market remains restricted principally to stock listed on a foreign exchange or traded in foreign over-the-counter sales and markets specified by JASDA. Nevertheless, a number of Japanese subsidiaries of foreign companies (particularly U.S. companies) have made use of it as an effective means to expand their capital with incidental benefits for their parent companies which are able to improve their asset position. This article seeks to describe the practical requirements of a Japanese OTC registration for the foreign-managed Japanese company which wishes to take advantage of this opportunity.

I. GENERAL SITUATION AND PAST DEVELOPMENTS

OTC securities are classified into a “registered issue,” “controlled over-the-counter issue” and “blue sky issue.” A “registered issue” is stock registered with JASDA and handled in a market created mainly electronically among member securities dealers by JASDA with the assistance of the Japan Over-the-Counter Securities Company. “Registered issue” stock is divided into “basic rule registered issues” and “special rule registered issues” in accordance with the standards prescribed for its registration. A “controlled over-the-counter issue” is a very limited category involving stock permitted to be handled due to some special reason, such as continued transactions in shares delisted from an exchange. The term “blue sky issue” refers to all shares not falling within the prior two general categories. However, securities dealers are required by self regulation to avoid transactions in “blue sky issue” shares.

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art. 2 (1).
4. Listing upon a Japanese securities exchange remains, of course, another possible (but difficult) alternative.
5. Regulations Concerning Trading in Foreign Securities (Foreign Securities Handling Regulation), JASDA Fair Practice Regulation No. 4, established December 4, 1973 and as amended through February 18, 1998, arts. 7 (i)-(ii). 9. An older English translation is contained in JASDA REGULATIONS 135.
The strong and highly active growth of all aspects of the market in stocks during the 1980s with some eight hundred different registered issues on the over-the-counter market by September 1997, culminating in the sudden fall in sales in 1992 and 1993 and marred by scandals such as the 1988 Recruit Cosmos case, brought about the need for JASDA to further regularize and tighten its requirements.

Significant among the changes were: strengthening the rules on allotting a capital increase to third parties prior to going public and the disclosure of their names (December 1988); disclosure of transfers in shares of stock prior to going public (December 1988); requiring third parties allotted a capital increase to hold their allotted shares for a fixed period after going public (December 1988); introduction of a partial competitive bid system to determine the opening price.
(December 1988) and later improvement of its operation (December 1992); mechanization of the market by introducing the JASDAQ (Japan Securities Dealers Association Quotation) System including an online JASDAQ INDEX in real time (October 1991); imposition of restrictions on unfair practices in accordance with the July 1992 amendment of the Securities Exchange Law;\textsuperscript{11} reform of the disclosure system (Fall 1992); improvement of the system of JASDA review required prior to the registration of an issue (July 1994); establishment of the requirement that the company whose stock is registered name an officer in charge of disclosure of information and a staff member responsible for business contacts with JASDA to handle matters that must be disclosed (July 1994); requirement of disclosure concerning acquisitions by a company of its own registered issue (e.g. for transfer to its employees) (October 1994); dissemination of wide-spread knowledge concerning the Ministry of Finance's guidance respecting insider trading (March 1995); establishment of a system of special rule registered issues ("frontier issues") (July 1995); lessening of restrictions on soliciting investment in unregistered stock (July 1997); introduction of the "book building" format as an alternative to partial competitive bidding to determine the opening price (September 1997);\textsuperscript{12} and introduction of systems of credit and date-of-issue transactions as measures to improve the sale of shares in the resale market (October 1997).

II. ELIGIBILITY TO BE REGISTERED FOR THE OVER-THE-COUNTER MARKET IN JAPAN

A. Basic Rule Issues

Normally, registration of an issue of shares with JASDA for the over-the-counter market by a Japanese company will be treated as a basic rule issue. Such a company must have (1) a net worth of at least 200 million yen and 2 million shares of stock issued and outstanding on the registration date plus (2) an average of at least 1 million shares outstanding in the business year prior to the year of registration, (3) provided that this business year was twelve months in duration and the trading unit is 1,000 shares.\textsuperscript{13}

\textsuperscript{11} By Law No. 87 of 1992.
\textsuperscript{12} This system is based upon a practice used in the U.S. NASDAQ market. JASDA OTC HANDBOOK 18.
\textsuperscript{13} Regulations Concerning the Registration of Over-the-Counter Sale of Valuable Securities and Publication of the Price, Etc. 店頭売買有価証券の登録及び価格の公表等に関する規則, JASDA Fair Practice Regulation No. 2 established June 18, 1976 and as amended through September 19, 1997, art. 5(1)(i), (iv) [hereinafter cited as "Fair Prac. Reg. 2"]; Detailed Rules Concerning the "Regulations Concerning the Registration of Over-the-Counter Sale of Valuable Securities and Publication of the Price, Etc." 『店頭売買有価証券の登録及び価格の公表等に関する規則』に関する細則, JASDA Detailed Rules Established June 18, 1976 and as amended through September 19, 1997, art. 3 (i), (iii) [hereinafter cited as Fair Prac. Reg. 2 Det. Rules]. English translations are contained in JASDA REGULATIONS 55, 79.
The shares required to be issued and outstanding on the registration date when a different size trading unit is employed are as follows.¹⁴

<table>
<thead>
<tr>
<th>Size of Trading Unit</th>
<th>Number of Shares Outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,000 shares</td>
<td>2,000,000 shares</td>
</tr>
<tr>
<td>100 shares</td>
<td>2,000,000 shares</td>
</tr>
<tr>
<td>50 shares</td>
<td>100,000 shares</td>
</tr>
<tr>
<td>10 shares</td>
<td>20,000 shares</td>
</tr>
<tr>
<td>1 share</td>
<td>2,000 shares</td>
</tr>
</tbody>
</table>

The company must have also adopted a trading unit unless the company was established on or after October 1, 1982.¹⁵ This trading unit is determined by the same rules that govern shares on a Japanese exchange (i.e., one unit is the number of shares whose total par value equals 50,000 yen).¹⁶ The trading unit for shares with a par value of yen is 1,000 shares—still a common situation in Japan. In effect, the trading unit for shares of a par value of 50,000 yen would be one share. While we describe this situation as a “trading unit,” strictly speaking, the rules of JASDA refer to it as a case where a trading unit is not required since only one share is involved. Thus, companies established on or after October 1, 1982 will have set the par value of its shares at 50,000 yen and will act the same as if the trading unit is one share. Accordingly, the average number of shares outstanding in the prior business year must have been as follows:

<table>
<thead>
<tr>
<th>Size of Trading Unit</th>
<th>Number of Shares Outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,000 shares</td>
<td>1,000,000 shares</td>
</tr>
<tr>
<td>100 shares</td>
<td>1,000,000 shares</td>
</tr>
<tr>
<td>50 shares</td>
<td>50,000 shares</td>
</tr>
<tr>
<td>10 shares</td>
<td>10,000 shares</td>
</tr>
<tr>
<td>1 share</td>
<td>1,000 shares</td>
</tr>
</tbody>
</table>

The net profits of the company (the lower of the figure prior to tax or the figure for ordinary profit) for the immediately prior business year of twelve months must have been at least 10 yen per share when the trading unit is 1,000 shares calculated by dividing profit for this period by the average number of shares outstanding during the period. If a different trading unit is used, the income per share figure must be 10,000 yen divided by the number of shares in the unit (e.g. 10,000 yen profit for a unit of 50,000 yen).¹⁸

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¹⁴ Fair Prac. Reg. 2, art. 5 (1) (i).
¹⁵ Fair Prac. Reg. 2, art. 5 (1) (vi).
¹⁶ See e.g. Operating Rules 業務規程, Tokyo Securities Exchange established April 1, 1949 and as amended through January 1, 1995, art. 150(11); Law Amending Part of the Commercial Code 商法の一部を改正する法律, Law No. 74 of 1981, Supp. Prov. art. 16(1) [hereinafter cited as “1981 Com C Amend L”].
¹⁷ Japanese law permits a business year to be less than twelve months, but all business year figures required as a registration requirement must be determined on a twelve month basis. See COMMERCIAL CODE 商法, Law No. 49 of 1890 [hereinafter cited as COM C], art. 33 which requires closing the books at least once a year, but does not prohibit closing on the basis of a period shorter than twelve months.
¹⁸ Fair Prac. Reg. 2, art. 5 (1) (iii); Fair Prac. Reg. 2 Det. Rules art. 3 (i)–(ii); Regulations Concerning the Terms, Form and Method of Preparing Financial Statements, Etc. 財務諸表の用語、様式及び作成
No express requirement for registration is imposed concerning the payment of dividends, but the rules governing the underwriting of a capital increase through public subscription do require that a satisfactory level of dividends must be shown and published in accordance with a definite basic dividend policy before underwriting will be undertaken. Prior to 1996, even more specific rules were in force, and in some cases they may still apply to companies whose stock was registered prior to April 24, 1996. These rules prescribed that:

1. (a) A level had to be established as to the standard rate at which it could be anticipated dividends would increase in the future (called a "standard propensity for dividends"). (b) This propensity was required to be not less than 30 percent. (c) Confirmation of a course endeavoring to maintain this propensity had to be confirmed by what was called a "public promise" to continue to meet the standard. (d) The issuing company was required to publicly announce this action.

2. If the company's average rate of profit on shareholder capital had exceeded 8 percent for the prior two business years before the year of the application date, the standard propensity for dividends required was not governed by the 30 percent provided above, but by a figure computed by dividing 2.4 percent and four tenths by the average rate of profit on shareholder capital. Here, "average rate of profit on shareholder capital" meant the total of the net profit for the past two business years divided by the total of the year-end figures for average shareholder capital for the same past two business years.

3. The public promise had to be maintained for a period of three years from the closing date of the business year which arrived after the day following the paying-in date for the stock.

4. A dividend to be taken into account in the computation was presumed to occur on the date of a stock split.

Method Concerning the Distribution of Profit of an Issuing Company to Be Observed by Association Members Upon Underwriting, published by JASDA Fair Practice Regulation No. 14 established May 13, 1992 and as amended through August 8, 1997, art. 6 [hereinafter cited as "Underwriting Rules"]. An older English translation is contained in JASDA Regulations 299.

In re the Matter Concerning the Distribution of Profit of an Issuing Company to Be Observed by Association Members Upon Underwriting, Resolution of the Board of Governors, JASDA, adopted March 24, 1992 and rescinded April 24, 1996; Provisional Measures Concerning the Abolition of "In re the Matter Concerning the Distribution of Profit of an Issuing Company to Be Observed by Association Members Upon Underwriting" published by JASDA, Resolution of the Board of Governors, JASDA, adopted April 24, 1996.
5. If the dividend per share met any of the following conditions during the public promise maintenance period, it would be deemed that the required standard propensity for dividends had been met in that business year:

a. There was an increase of not less than 20 percent in the dividend over the prior business year and the propensity for dividends result for the prior year was not less than 20 percent.

b. There was an increase of not less than 20 percent in the dividend over the prior business year and the propensity for dividends result for the prior year was not less than the figure computed under 2 above.

c. There was an increase of not less than 30 percent in the dividend over the prior business year and the propensity for dividends result for the prior year was not less than 10 percent.

6. Net profit in making the above computations did not include any special profit.

7. The underwriting securities companies were required to publicly announce the above matters in a short communication after they were determined and in other materials published later at an appropriate time. They were also required to make a report to JASDA on a prescribed form concerning the status of maintaining the publicly promised propensity for dividends.

8. JASDA was to compile in turn the reports of 7 above and publish them.

Requirements are imposed as to the number of shares offered for public sale and the distribution of shares held within Japan prior to registration. The shares offered for public sale must be as follows, assuming a trading unit of one thousand shares:

<table>
<thead>
<tr>
<th>Stock Outstanding on the Registration Application Date</th>
<th>Public Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 500,000 shares</td>
<td>500,000 shares or more.</td>
</tr>
<tr>
<td>500,000 shares or more</td>
<td>12.5% of the outstanding shares plus 250,000 shares.</td>
</tr>
</tbody>
</table>

21. Fair Prac. Reg. 2, art. 6 (2).
22. However, a special determination may be made by JASDA for companies with a very large number of shares already outstanding. Fair Prac. Reg. 2, art. 6 (3).
When the trading unit is one share (50,000 yen par value), the requirements become:

<table>
<thead>
<tr>
<th>Stock Outstanding on the Registration Application Date</th>
<th>Public Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 500 shares</td>
<td>500 shares or more</td>
</tr>
<tr>
<td>500 shares or more</td>
<td>12.5% of the outstanding shares plus 250 shares.</td>
</tr>
</tbody>
</table>

The number of persons holding one or more trading units in the company must be as follows at the time of registration:

<table>
<thead>
<tr>
<th>Stock Outstanding on the Registration Date</th>
<th>Number of Persons</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Less than 20,000,000 shares (trading unit 1,000)</td>
<td>200</td>
</tr>
<tr>
<td>Less than 20,000 shares (trading unit 1)</td>
<td></td>
</tr>
<tr>
<td>2. 20,000,000 shares or more (trading unit 1,000)</td>
<td>400</td>
</tr>
<tr>
<td>20,000 shares or more (trading unit 1)</td>
<td></td>
</tr>
</tbody>
</table>

The most recent Audit Report must reflect the opinion of a certified public accountant or audit juridical person that it is "correct" or "expresses useful accounting information" and that it is not generally subject to any exceptions.

The form of share certificates issued by the company must comply with standards set by JASDA.

No restrictions may be placed on the assignability of shares except those prescribed by law for companies in certain specified forms of business. The company applicant must commission a title transfer agent from among those designated by JASDA to handle financial relations with its shareholders.

Finally, the company must not be listed on a Japanese securities exchange nor have had an over-the-counter registration cancelled within three years prior to the date of the application for registration, and it must provide in its Charter for public notices to be published in a daily newspaper.

B. Special Rule Issues

Registration of special rule issues (sometimes called "frontier issues") grew out of recognition of the need to develop a system to provide capital for new high-tech Japanese companies. This occurred by not requiring quite as stringent requirements
as had been imposed hitherto and are still a condition for basic rule issues. Founded
upon a report concerning over-the-counter registration special rule issues29 of a
special body created by JASDA, the relevant regulations were amended on July 19,
1995,30 and the change was approved by the Minister of Finance in accordance with
the Securities Exchange Law.31

In order for a company to be eligible to register a special rule issue it must be
involved in a new industry with good prospects for the future. It need not meet the
quantity of shares outstanding and ten yen per share net profit requirements imposed
on a basic rule issue. However, the ratio of its sales to expenses needed to operate its
business in the new field must be 3 percent or more and it must have a net worth of
200 million yen or more as well as at least fifty or more shareholders on the date of
registration.32 Moreover, there is a requirement that there be a minimum of 500,000
shares (assuming a trading unit of one thousand shares) offered for public sale.33

III. RESTRICTIONS ON THE USE OF STOCK OPTIONS
AND THE TRANSFER OF SHARES

The English word “option” has been brought into the Japanese language in the
past half century as a catch-all term to cover certain rights significant in and limited
to securities law. The Japanese civil law34 system uses the word “precontract”35 for
what is called an “option” in the common law.36 However, “stock option”37 has
been increasingly used in connection with securities to cover two technical legal
concepts: the right to accept new shares38 and a contractual right to buy treasury
shares39 from a company. Accordingly, it is not the same as the legal concept of an
“option” under the common law. Thus, any legal analysis of stock options and their
effect must be determined upon the basis of whether the right to accept new shares
or a contractual right to treasury shares is involved. This is also true in regard to
understanding the meaning of “warrant,”40 which has recently become popular in
Japan to refer to a form of the right to accept shares that have been issued to the
officers or employees of a company.41

29. Tentô Toroku Kijun Kentô Tô Kondankai 店頭登録基準検討等 魅論会 (Over-the-Counter
Registration Standards Investigation, Etc. Consultative Committee), Tentô Toroku Tokusoku Meigara Seido ni
Tsute 店頭登録特則 魅論制度 について (In re an Over-the-Counter Registration Special Rule Issues
System) (June 21, 1995).
31. See Securities Exchange Law art. 76; JASDA OTC HANDBOOK 41.
32. Fair Prac. Reg. 2, art. 5-2; Fair Prac. Reg. 2 Det. Rules art. 3 (viii)-(ix).
33. Fair Prac. Reg. 2, art. 6 (4).
34. Called “continental law” in Japan in accordance with European practice.
35. Yoyaku 予約. See CIVIL CODE, Laws No. 89 off 1896 and No. 9 of 1898, arts. 556, 589 [hereinafter
cited as CC].
36. Called “Anglo-American law” in Japan also in accordance with European practice.
37. Stokku opushon ストックオプション.
38. This is a form of right created by the Commercial Code. See COMC arts. 190, 280-9-280-22.
40. Warrantoワラント.
41. See “success compensation type warrants” and “success compensation debenture type warrants” as
defined on page 13 infra.
It used to be a common practice in Japan, for companies issuing new shares, pursuant to an expansion of capital and Japanese securities companies assisting in such an offering, to provide persons whom they wished to reward, at little cost to themselves as reported for accounting purposes, with an award of the right to purchase new shares at the current market price at the time of the award. The price of these new shares were usually substantially below the value to which the stock always rose soon after being placed for public sale (the Commercial Code requires a two thirds vote of the board of directors and a special report to the shareholders disclosing the reason in such a case). This stock would then be acquired and resold at great profit to its initial owner a few days after the initial public offering. It is this practice which gave rise to the Recruit Cosmos scandal where this device was widely utilized by favored politicians. Equally, insiders within the company issuing the stock would often take advantage of the same opportunity.

Guidelines were adopted in March 1988 by the Over-the-Counter Section, Operations Division, JASDA, to deal with the situation. However, these provisions were criticized as being too vague. They were ultimately replaced by a much stricter body of restraints based upon the government's Securities Exchange Council report of December 21, 1988, entitled In re What Ought to Be the Going Public System for Stock. The new restrictions were adopted pursuant to Fair Prac. Reg. 2, art. 5 (1) (xiii) and are known as the Rules Concerning a Capital Increase Allocated to a Third Party and Stock Transfers of a Person with a Specially-Related Interest, Etc. Prior to Registration.

No company may register its stock with JASDA for sale if it violates these provisions. A violation during the course of processing an application for registration will result in termination of the application. Similarly, a violation after an issue is registered may result in JASDA ordering its members to cease engaging in transactions involving the shares.

The rules provide a very broad net to cover those having a close connection with a company seeking to register an offering of a new issue of its stock with JASDA on the over-the-counter market (called a "registration applicant company"). The rules then proceed to severely limit the grounds upon which these parties may make use of a new stock option concerning shares to be offered or the basis upon which they may transfer any shares in the registration applicant company that may be currently held by them.

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42. COM C arts. 280-2 (2), 343.
44. JASDA Rule established March 8, 1989 (hereinafter cited as the "Third Party Capital Increase Allocation Rules").
45. Third Party Capital Increase Allocation Rules arts. 3 (1)-(2), 3-2 (1).
The following are definitions of the key terms employed in these rules:

*Capital increase allocated to a third party.* Any issuance of new shares of stock by a company pursuant to an increase in its capital other than shares allocated to existing shareholders.⁴⁷

*Capital related company.* Any of the following qualify:⁴⁸
1. Another company in which a registration applicant company substantially owns 20 percent or more of the outstanding shares of stock.
2. Another company in which a person with a specially-related interest with a registration applicant company substantially owns 20 percent or more of the outstanding shares of stock.
3. Another company which substantially owns 20 percent or more of the outstanding shares of stock of a registration applicant company.
4. Another company with which there is a person with a specially-related interest who substantially owns 20 percent or more of the outstanding shares of stock of a registration applicant company.

*Major shareholder.* A person who owns 10 percent or more of the outstanding shares of a company in his own name or through the name of another.⁴⁹

*Member, etc.* A securities company which is a member of JASDA (including a foreign securities company), its officers and a capital related company or personally related company of such a securities company as the company determining the relationship instead of the registration application company. However, a company which substantively owns 20 percent or more of the outstanding shares of a securities company is not included within this term if JASDA has concluded that failure to do so does not present an obstacle to maintenance of fairness in going public with the stock involved in the registration.⁵⁰

*Person with a specially-related interest.* Any "officer, etc." of a registration applicant company, company in which such an "officer, etc." owns more than half of the total outstanding shares and "related company" as this term is defined in the Financial Statement Regulations⁵¹ pursuant to the Securities Exchange Law.⁵² An "officer, etc." refers to an officer, his or her spouse and his or her relatives within the second degree of relationship as defined by the Civil Code.⁵³

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⁴⁷ Third Party Capital Increase Allocation Rules art. 2 (i). This activity constitutes a "solicitation" under Securities Exchange Law art. 4.
⁴⁸ Third Party Capital Increase Allocation Rules art. 2 (v). See also Ministerial Order Concerning Disclosure of the Content of a Business, Etc., Ministry of Finance Order No. 5 of 1973, art. 1 (xxxi) (c) [hereinafter cited as "Disclosure Min. O."].
⁴⁹ Third Party Capital Increase Allocation Rules art. 2 (vii). See also Securities Exchange Law art. 163 (1) (referring to holding through a "nominee" 仮設人).
⁵⁰ Third Party Capital Increase Allocation Rules art. 2 (xi).
⁵¹ Financial Statement Regulations art. 8 (5).
⁵² Securities Exchange Law art. 5; Disclosure Min. O. art. 1 (xxxi) (a).
⁵³ CC art. 725.
The word "officer" itself means a director, statutory auditor and persons comparable thereto and also includes here an "officer stock holding society." 

_Persons with a specially-related interest, etc._ Any of the following: (1) a person with a specially-related interest with a registration applicant company; (2) a personally related company and a capital related company of a registration applicant company and the officers of these types of companies; (3) the ten senior large shareholders of a registration applicant company; and (4) a member, etc.

_Personally related company._ A company substantially controlled by a registration applicant company or that substantially controls a registration applicant company by means of relationships involving such matters as personnel, funding, technology or transactions, etc.

_Senior capital company._ Another company (other than a member, etc.) which substantively owns 20 percent or more of the outstanding shares of stock of a registration applicant company.

_Sister company._ A company (other than a member, etc.) that is not a registration applicant company in which a senior capital company substantively owns 20 percent or more of the outstanding shares of stock.

_Specially-designated shares._ Shares issued as new shares by the registration applicant company to a director or employee at a particularly advantageous issue price upon the director’s or employee’s exercise of a right to accept new shares allocated to him or her for an appropriate reason.

_Subsidiary company._ A company in which the registration applicant company owns more than half the voting rights.

_Success compensation type warrant._ A right to accept new shares, which has been issued in the form of a security and separated from a success compensation debenture type warrant issued by the registration applicant company.

_Success compensation debenture type warrant._ A debenture with an attached right to accept new shares issued by the registration applicant company for the purpose of assigning a right to accept new shares, which has been issued in the form of a security to an officer or employee of the company or its subsidiary as compensation, salary or a bonus and where this security has been redeemed from its underwriter.
Ten senior large shareholders. The top ten shareholders in the order of their ownership of the largest number of shares in a company. 64

The JASDA restrictions make a distinction between shares issued pursuant to a "capital increase allocated to a third party" by the registration applicant company and a transfer of shares already held by an existing shareholder.

The former case involves an allocation of the right to purchase new shares as well as the conversion of a convertible debenture or the exercise of a right to acquire new shares attached to a debenture, except where expressly stated to the contrary. 65 A further distinction is made in this case between normal shares and specially-designated shares. The rules have established a prohibited period for normal shares and a restricted period for both types of shares during which different restraints apply.

The prohibited period for normal shares extends from the date, following the day six months prior to the closing date of the books of the registration applicant company immediately prior to the date application is made to register an issue for sale (i.e. the "application date"), until the day before the date of registration. 66 The restricted period for normal shares runs from the date, following the day two years prior to the closing date of the books of the registration applicant company immediately prior to the application date, until the beginning day of the prohibited period one year and six months later. 67 The restricted period for specially-designated shares begins on the same date as for normal shares but runs until the day before the date of registration. 68

No third party allocated capital increase regarding normal shares may take place during the prohibited period. The day following the day of paying-in for the stock is defined to be the "date of the increase in capital." 69

During the restricted period, a capital increase allocated to a third party involving normal shares may take place only if the issue price is at least 80 percent (70 percent in the case of an allocation to an employee stock holding society) of the price of stock of a comparable company as determined by a specified formula. 70

Moreover, if the allocation involving normal shares is made to persons with a specially-related interest, it may be done only in the following cases provided that the JASDA deems the capital increase to be appropriate: 71

1. The case of an allocation either to a senior capital company (other than a company in which its officers, etc. own more than half of its outstanding shares) of the registration applicant company or to a sister company (other than a company which is a person with a specially-related interest with the registration applicant company) of the registration applicant

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64. Third Party Capital Increase Allocation Rules art. 2 (vi); Disclosure Min. O. art. 1 (xxxi) (b).
65. Third Party Capital Increase Allocation Rules art. 2 (i).
66. Third Party Capital Increase Allocation Rules art. 3 (1).
67. Third Party Capital Increase Allocation Rules art. 3 (2).
68. Third Party Capital Increase Allocation Rules art. 3-2 (1).
69. Third Party Capital Increase Allocation Rules art. 3 (1).
70. Third Party Capital Increase Allocation Rules art. 3 (2) (i); Fair Prac. Reg. 2, art. 7; Fair Prac. Reg. 2 Det. Rules art. 4 (1) (iii), Sep. Sch. 2.
71. Third Party Capital Increase Allocation Rules art. 3 (2) (ii).
company, where the percentage of shares to be owned after the capital increase out of the total outstanding shares of the registration applicant company is not greater than the percentage of such shares owned by the said senior capital company or sister company prior to the increase. Where the registration applicant company has issued convertible debentures or debentures with an attached right to accept new shares, the percentage of shares owned is computed by (1) dividing the number of shares which is the total of (a) the number of shares owned and (b) the number of shares that could be acquired through the conversion of the convertible debentures, debentures with an attached right to acquire new shares and the rights to acquire new shares in the form of a security or the exercise of rights to acquire new shares in behalf of the senior capital company or sister company by (2) the total of (a) the number of shares issued and outstanding from the registration applicant company and (b) the number of shares that could be issued to date as a result of the conversion of all convertible debentures and debentures with an attached right to acquire new shares or the exercise of rights to acquire new shares.

2. The case of an allocation to a major shareholder (other than a person with a specially-related interest with the registration applicant company and such person’s officers, when this person is a company) of the registration applicant company where the percentage of shares to be owned after the capital increase by this shareholder out of the total outstanding shares of the registration applicant company is not greater than the percentage of such shares owned prior to the increase.

3. The case of an allocation to one of the ten senior large shareholders where the percentage of shares to be owned after the capital increase by the shareholder is not greater than 10 percent of the total outstanding shares of the registration applicant company. However, this shareholder may not be: (1) a person with a specially-related interest with the registration applicant company; (2) a member, etc.; (3) a personally related or capital related company of the registration applicant company; (4) the officers of such a person with a specially-related interest, personally related company or capital related company; (5) or a person listed in 1 and 2 above or 4 below.

4. The case of an allocation to an officer of the registration applicant company or an officer of its subsidiary company where the number of shares held by the officer after the allocation will not exceed 10,000 shares when the trading unit is 1,000 (10 shares with a trading unit of 1 share). However, where the person accepting the allocation owns shares issued as specially-designated shares or through the exercise of a right to accept new shares under a success compensation type warrant which shares have been placed on deposit as described below, these shares are to be excluded from the 10,000 shares. On the other hand, convertible debentures, debentures with an attached right to accept new shares and rights to accept new shares in the form of a security (other than success compensation debenture type warrants placed on deposit) shall be included.
The case of an allocation to a person whose purpose is to conduct the business of investing in a small or medium-sized enterprise in order to promote the adequacy of this enterprise's own capital and its healthy growth and development provided that the number of shares allocated is perceived to be appropriate for this purpose.\textsuperscript{72}

None of the above restrictions apply to a capital increase allocated to a third party concerning specially designated shares.

A person allocated a capital increase during the restricted period, the registration applicant company, and the securities companies applying to JASDA for registration of the issue of shares must all enter into a written compact concerning the rights acquired. In the case of normal shares this compact shall contain a promise that the person allocated the rights will in principle continue to hold ownership of the shares received through the exercise of the rights until a date one year from the registration date and that the share certificates will be deposited with the applicant securities companies until that time.\textsuperscript{73} The same basic rule concerning holding ownership and deposit of the share certificates also applies to specially-designated shares. However, the holding and deposit need last only until the day before the registration date.\textsuperscript{74}

Other promises required to be entered in the written compact for both normal and specially-designated-shares are that:

1. The person allocated a capital increase will report promptly to the registration applicant company any assignment of the shares or receipt of the return of the share certificates during the restricted period.

2. The applicant members will report promptly to the registration applicant company the content of any demand for return of the share certificates on deposit from the person allocated the capital increase and the actual return thereof.

3. Upon an assignment during the restricted period the registration applicant company will report in writing to the applicant member the names and addresses of any persons assigning and receiving an assignment of stock, the number of shares, the assignment price, the date of the assignment, the reason for the assignment and other necessary matters, and upon a return of shares during the restricted period the names and addresses of any persons receiving the return of share certificates, the number of shares, the date of the return, the reason for the return and other necessary matters. These reports will be made at the time of the registration application, when the event occurs before the registration application.

\textsuperscript{72} This provision is directed at venture capital operations. JASDA OTC HANDBOOK 29.

\textsuperscript{73} Fair Prac. Reg. 2, art. 32 (1)-(2); Fair Prac. Reg. 2 Det. Rules art.16; Third Party Capital Increase Allocation Rules arts. 3 (2) (iii), (3)-(4). See infra 12, and 13 on page 30 below.

\textsuperscript{74} Third Party Capital Increase Allocation Rules art. 3-2 (1)(i). Model forms to be used for this compact will be found in KAISHA JÔHÔ TEKUJI KADII NO TEBIKI KÔSÔSHI NO HANTEI (Company Information Disclosure at the Proper Time Handbook) 93 (Nihon Shôken-gyô Kyôkai Japan Securities Association rev. ed. 1998) [hereinafter cited as JASDA DISCLOSURE HANDBOOK].

\textsuperscript{75} Third Party Capital Increase Allocation Rules arts. 3 (1)(iii)(b)-(g), 3-2 (1)(ii).
date, and promptly after the assignment or registration if they occur after that date.
4. The applicant members will submit copies of the reports in 3 to JASDA at the time of the registration application if received before that date or promptly if received after that date.
5. The person allocated a capital increase will provide the content of the aforesaid assignment of shares or return of certificates for inspection by the public.
6. The parties will comply with other matters perceived necessary by JASDA. Restrictions on the transfer of previously held shares of stock are governed by somewhat different rules.

JASDA has set a transfer restricted period, extending to the day before the registration date from the day after the date two years prior to the closing date of the books of the registration applicant company immediately prior to the registration application date. During this time, a person with a specially-related interest, etc. with the registration applicant company may not transfer any shares of stock unless the transfer is deemed appropriate by JASDA and the transfer falls within one of the following cases:76

1. An assignment or receipt of assignment of shares between a person with a specially-related interest, etc. with the registration applicant company or a relative of this person. The price of the shares may be freely determined between the parties.
2. An assignment or receipt of assignment of shares between a person with a specially-related interest, etc. and the registration applicant company based upon any of the following events: acquisition of fractional shares;77 acquisition by the company of the shares of a shareholder opposed to selling a business, authorization of the transfer of assignment restricted shares, a merger or the change of a limited liability company into a stock company;78 acquisition of shares under a preferred right to purchase;79 acquisition by the company of shares to become treasury shares for assignment to employees;80 acquisition by the company of assignment restricted shares from an heir;81 acquisition by the company of shares for their retirement;82 and, acquisition of shares by a shareholder to fill a gap in a trading unit.83
3. An assignment or receipt of assignment of shares between a senior capital company and a sister company of the registration applicant company (intergroup transfer).

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76. Third Party Capital Increase Allocation Rules art. 5 (1).
77. Com C arts. 210 (iv), 230-8-2 (2).
78. Com C arts. 210 (iv), 245-2 (2), 349 (1), 408-3; Limited Liability Company Law 有限 会 社 法, Law No. 74 of 1938, art. 64-2 (1).
79. Com C arts. 210 (v), 204-3 (1), 204-5. This right is equivalent to a right of first refusal in US law.
80. Com C art. 210-2 (1).
81. Com C art. 210-3 (1).
82. Com C art. 212-2 (1).
4. An assignment or receipt of assignment of shares between sister companies of the registration applicant company (intergroup transfer).

5. A receipt of assignment of shares by an officer of the registration applicant company or of its subsidiary company where the number of such shares held after the assignment does not exceed 10,000 shares when the trading unit is one thousand shares (10 shares where the trading unit is one). The 10,000 shares do not include specially-designated shares and shares issued due to the exercise of a right to accept new shares of a success compensation type warrant which have been placed on deposit with the applicant securities companies, but do include the number of shares that could be acquired by the conversion of a debenture or exercise of the right to accept new shares under rights to acquire new shares in the form of a security or a debenture with an attached right to acquire new shares.

6. An assignment or receipt of assignment of shares by a person with a specially-related interest, etc. (excluding a member, etc.; the same hereafter in 7, 8, 10 and 11 of this list) with the registration applicant company in order for the former to strengthen or extinguish a business operating connection with that company.

7. An assignment or receipt of assignment of shares between another person and a person with a specially-related interest with a registration applicant company in order to strengthen or extinguish a business operating connection between the registration applicant company and the other person.

8. A receipt of the assignment of shares in a registration applicant company by a person with a specially-related interest from an officer of this company due to his or her ceasing to be an officer.

9. An assignment of shares in a registration applicant company by a person with a specially-related interest due to his, her or its marked inactivity in the business.

10. An assignment or receipt of assignment of shares by a person with a specially-related interest with the registration applicant company upon that company having so directed in writing based on the needs of the capital policy of the company or on another proper reason.

11. An assignment of shares by a person with a specially-related interest to an employee stock holding society of the registration applicant company.

12. Other assignments or receipts of assignment recognized to be unavoidable from the standpoint of the common sense of society.

Except for 1 and 2 above, the price to be paid for the shares will be that computed from the price of stock of comparable companies as noted on pages 14-15 above.

84. Third Party Capital Increase Allocation Rules arts. 5 (1)(v), 3-2 (1), 7 (3).

85. However, success compensation type warrants placed on deposit with an applicant securities company are not included. Third Party Capital Increase Allocation Rules arts. 5 (1)(v), 7 (1).

86. Third Party Capital Increase Allocation Rules art. 5 (2)).
IV. REGISTRATION OF SHARES

A. In General

A foreign-related Japanese domestic company seeking to be registered for sales of its stock on the over-the-counter market in Japan will normally begin by contacting an international law firm, with a presence and authorized to practice law in Japan. This law firm will provide an evaluation of the company’s prospects to proceed. Assistance from two or more Japanese securities companies, which are members of JASDA, and two certified public accountants or one audit juridical person will also be required.

The need for the law firm lies in its ability to provide objective independent advice and monitoring during the application and post-application process. This is done in a confidential manner solely in the interest of the applicant client subject to the legal professional’s code of ethics. The law firm assists in the preparation of various statements and reports required to be filed with the Ministry of Finance under the Japanese Securities Exchange Law. The law firm is also often very helpful in assisting the applicant in preparing its application documents in such a way as to maximize the probability of a successful registration. Thus, the key to the lawyer’s role is that his or her sole goal is the client’s success. Lawyers with extensive experience and influence in Japanese finance and government regulation of securities matters can be particularly helpful.

The role of the securities companies is to make the formal application for registration with JASDA. In this connection, they will conduct a careful review as to the acceptability of the company’s stock for registration, arrange for the underwriting of the securities to be registered and furnish a large staff of personnel who will be able to assist in speeding up the preparation of the complex and very detailed portions of the registration documents. The selection of these applicant securities companies should be weighed carefully. Some tend to approach the registration task as a volume operation much in the same fashion as Japanese general trading companies deal in a very large variety of many different products. Accordingly, they seek to undertake the registration task for many companies, but their efforts are sometimes quite mechanical and not tailored to the particular needs and success of the company applicant for which they are acting. Others specialize in providing more extensive service and guidance and often, in my opinion, have a “we try harder attitude.” The close connections of a securities company with major financial institutions, such as insurance companies and banks, which may purchase or support the sale of the stock should also be carefully considered. For example, until recently none of the big three securities companies had as close bank connections as many in the tier of securities companies just below this top level.

As the formal application for over-the-counter registration must be submitted to JASDA in the names of the applicant securities companies, the first step for a foreign-related Japanese domestic company seeking registration of its shares on the OTC market is to determine the law firm and the securities companies whose assistance it will need.
Conduct of an Initial Public Offering in Japan

Two or more of the securities companies will act as "managing securities companies." JASDA statistics indicate that of the 137 companies registering in the banner year of 1995 and the 102 companies registering in 1997 as many as ten managing securities companies were selected on the average by each registration applicant company. One among all the participating securities companies must also be designated by the managing securities companies as the "representative applicant member" of JASDA. Normally, the company receiving this designation will in fact be selected by the registration applicant company, although formal selection is done by all the managing securities companies.

Care should be taken in selecting all of these managing securities companies for the reasons stated above and because it is important that the registration applicant company exercise its independent judgment in selecting the supporting companies and not simply accept the recommendation of one lead company.

<table>
<thead>
<tr>
<th>Table II</th>
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<tbody>
<tr>
<td>GROWTH IN THE NUMBER OF MANAGING SECURITIES COMPANIES SELECTED BY COMPANIES MAKING AN OVER-THE-COUNTER REGISTRATION</td>
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<tr>
<td>1988-1997</td>
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<tr>
<td>Number of Managing Companies for Each New Registrant OTC Company</td>
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<td>(53)</td>
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<tr>
<th>Number of OTC Company</th>
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<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
<th>11</th>
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<td>1997</td>
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<td>7</td>
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</table>


The role of the certified public accountants or audit juridical person is to prepare the newly required audits together with supporting and information documents.

87. Fair Prac. Reg. 2, art. 3. "Managing securities company" is used here to translate 潜事証券会社.

88. Fair Prac. Reg. 2, art. 8-2. This company is also commonly referred to as the "lead [literally "principal"] securities company" 主幹事証券会社.

89. See 1 on page 31 infra regarding the consent to be filed by the registration applicant company.
B. Bidding vs. Book Building

Determination of the opening price of shares upon registration is a very important matter. Formerly, this determination was always made by a competitive bidding system initiated in 1988 and subsequently revised in 1992. However, in September 1997, a book building system modeled on practice in the United States was introduced as an alternative. Now book building must always be used for special rule issues. Otherwise, selection is at the discretion of the applicant securities company and the underwriters.

Under the bidding system, the registration applicant company and the applicant securities companies work out a minimum bid price based upon multiplying 85 percent times a figure derived from comparison with similarly situated companies. Actual conduct of the bidding is delegated to JASDA. Competitive bids are solicited for the purchase of 50 percent or more of the shares of stock subject to the public offering. The result is then used to work out a weighted average which becomes the opening price. If less than 25 percent of the shares are bid upon, the bidding is cancelled.

Book building takes a different approach to working out the opening price. It was introduced in Japan because it was thought that bidding, in its limitation of eligible bidders principally to individuals, failed to take into account the impact of prospective large-scale institutional and foreign investors who would drive up the price.

Under the book building system, the underwriters seek to work out provisional terms for the offering in consultation with the registration applicant company by comparing the applicant company’s results with that of other similarly situated companies. Taken into account are the content of the business, operating success and financial standing. The views of the managing securities companies, institutional investors and others with professional knowledge and experience are solicited. Other relevant opinions are also sought and examined.

The provisional terms (including price) are then tested by the underwriters with various possible customers to try to discover the degree of demand for the shares. Based upon these activities the opening price is fixed.

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90. Fair Prac. Reg. 2, art. 7 (1).
91. Fair Prac. Reg. 2, art. 7 (2).
92. Fair Prac. Reg. 2, art. 7 (3); Fair Prac. Reg. 2 Det. Rules art. 4-2 (1)(ii), Sep. Sch. 2. See page 14 above where this same system is applied.
93. Fair Prac. Reg. 2 Det. Rules art. 4-2 (1)(i).
94. Fair Prac. Reg. 2 Det. Rules art. 4-2 (1)(ii).
95. Fair Prac. Reg. 2, art. 7-2 (ii).
96. Fair Prac. Reg. 2 Det. Rules art. 4-2 (1)(v).
C. The Registration Process

The next steps leading to registration will then be as follows:

1. Establishment of a project team by the registration applicant company, consisting of key concerned personnel within the company, representatives of the applicant securities companies, lawyers and accountants, to assign responsibility for gathering and preparing documents and other necessary activities for the registration.

2. Study of and implementation of changes which will be required to be made within the registration applicant company in order to comply with the formal requirements for registration and to meet areas of concern that will be examined upon substantive review of the application.

3. A resolution by the board of directors of the registration applicant company to seek registration.

4. Preparation of a Valuable Securities Report for the Purpose of the Registration Application and a Report for the Purpose of the Registration Application by the registration applicant company with the assistance of the applicant securities companies, the lawyers and the accountants.

5. Careful substantive review by the applicant securities companies to make certain that the registration applicant company is qualified for registration.

6. Determination by the applicant securities companies that they will proceed and preparation by them of the Registration Applicant Company Written Investigation, and Report of Review as a result of the review in 5 above.

7. Filing with and acceptance by JASDA of a Registered Issue Written Registration Application indicating the state of compliance with the registration standards prepared by the applicant securities companies and accompanied by various attached documents including the Registration Applicant Company Written Investigation, Report of Review, Report for the Purpose of the Registration Application, and the Valuable Securities Report for the Purpose of the Registration Application.

8. A hearing before the Registration Review Division of JASDA of a presentation by responsible personnel in the applicant securities companies in which is explained in outline the business of the registration applicant company.

99. 登録申請のための有価証券報告書.
100. 登録申請のための報告書.
101. See pages 26-32 infra.
103. 登録申請会社調査書.
104. 審査報告書.
105. 登録銘柄登録申請書.
106. See Section V infra.
9. Review by the Over-the-Counter Registration Committee of JASDA based chiefly on written materials submitted and an outline presentation by the representative of the applicant securities companies.
10. Application by the applicant securities company for an issue code to be assigned.
11. Deliberation by the Board of Governors of JASDA, authorization of the registration and notice thereof.
12. First formal resolution of the board of directors of the registration applicant company to seek a capital increase and the public sale of additional stock not specifying the terms thereof (normally the same day or the day following the action in 11 above).
13. Preparation and filing of a Valuable Securities Statement, and an attached Preliminary Provisional Prospectus with the Securities Bureau of the Ministry of Finance through the competent regional Finance Bureau.
14. Second formal resolution of the board of directors of the registration applicant company to seek a capital increase and the public sale of additional stock including the terms thereof.
15. Preparation and filing of the first Corrected Valuable Securities Statement at the competent regional Finance Bureau before bidding or book building to determine the opening price of the shares, and commencement of the effectiveness of this statement.
16. Conduct of bidding or book building to determine the opening price.
17. Preparation and filing by the registration applicant company of a second Corrected Valuable Securities Statement at the competent regional Finance Bureau, taking into account the opening price of the shares as determined by bidding or book building, and commencement of the effectiveness of this Statement.
18. Setting of the period for subscription to a new issue and the paying-in date, and preparation of a report on the results after the specified dates have elapsed.
19. Issuance of notice of the registration date and commencement of transactions after that date.

D. Time Required for Registration

The period it will take to complete steps 1 through 6 described above will vary depending upon the readiness of the registration applicant company to proceed and its ability to meet the requirements set by JASDA (a number of which have lengthy time periods). JASDA itself suggests a probable term of three years divided as follows:

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107. 訂正有価証券届出書.
108. 訂正有価証券届出書.
1999 / Conduct of an Initial Public Offering in Japan

First Year
1. Establishment of the project team.
2. Selection of the managing securities companies.
3. Entering into an audit contract.
4. Study of the procurement of funds.
5. Study and reform of the composition of the shareholders of the registration applicant company.
6. Establishing a system of employee holding of shares, the creation of stable shareholders and dealing with the percentage of shares held by management in the registration applicant company.

Second Year
1. Completion of the management structure.
2. Preparation or modification of various internal company rules.
3. Study and reform of the organization of the registration applicant company.
4. Establishing adequate budgetary controls.
5. Establishing adequate internal audit.
6. Reform of the relationship of the registration applicant company with any related companies.

Third Year
1. Commencement of preparation of the registration application form.
2. Check of the state of applicability of the management structure of the registration applicant company.
3. Make changes in the par value of shares if needed.
4. Amendment of the Charter\textsuperscript{10} of the registration applicant company as needed.
5. Determination of the form of the share certificates.

The time required for the remaining major steps would be approximately as follows, "D" being the registration date:

\begin{itemize}
    \item \textbf{D - 78} Filing of the Registered Issue Written Registration Application with JASDA.
    \item \textbf{D - 57} Hearing in which the applicant securities companies explain in outline the registration applicant company before the Registration Review Division of JASDA, together with consideration of the Registration Applicant Company Written Investigation, Report of Review, Company Guide\textsuperscript{11} (including an Outline of the Company\textsuperscript{12}) and various pamphlets.
    \item \textbf{D - 55} Consultation regarding determining the opening price for the shares based upon the lowest bid price when the bidding system is used or within an appropriate band of prices when the book building system is used.
\end{itemize}

\textsuperscript{10} 定款.
\textsuperscript{11} 会社案内.
\textsuperscript{12} 会社概要.
Consultation regarding the Audit Summary\textsuperscript{113} to be issued by the auditors and the Valuable Securities Statement, etc.

The applicant securities companies discuss the Valuable Securities Report and the risk factor with the competent regional Finance Bureau of the Ministry of Finance (hereafter called the "Finance Bureau").

Hearing in which the applicant securities companies explain the distribution of profits to the Registration Review Division of JASDA.

Application for assignment of an issue code.

Review by the Over-the-Counter Registration Committee of JASDA, including receiving an explanation from the representative member and administrative personnel of JASDA together with taking into consideration the Registration Applicant Company Written Investigation and Company Guide.

Review and determination by the Board of Governors of JASDA to register, together with consideration of a Registration Applicant Company Written Investigation and the Company Guide.

First formal resolution of the board of directors of the registration applicant company to sell new shares without determining the terms thereof. Required documents are minutes of the meeting of the board of directors,\textsuperscript{114} a press release regarding the issue of new shares, etc. and a Written Estimate of When to Go Public\textsuperscript{115} (with a bidding advertisement, etc. if the bidding system is being used).

Publication of a notice of the resolution to issue new shares, announcement of the conduct of bidding, etc. and advertisement for the submission of bids (the latter two when the bidding system is being used).

Filing of a Valuable Securities Statement, a Preliminary Provisional Prospectus\textsuperscript{116} and a notice giving a summary of the makeup of sales on consignment (the last only in the case of the use of book building) with the Finance Bureau.

Receipt by the Underwriting or Underwriting Review Division of the applicant securities companies of a draft of the Audit Summary from the auditors.

Consultative meeting with the director of the company responsible for disclosure of information.

Prehearing in which representatives of the applicant company and representative securities company explain various concerns and answer questions.

Determination of the lowest bid price (if the bidding system is being used) or conduct of book building (when that system is being employed). At this point the Japan Over-the-Counter Securities Company notifies the result of the lottery to allocate shares on consignment (regarding book building).

Second formal resolution of the board of directors of the registration applicant company to sell new shares including the terms thereof. Required documents are: (1) Minutes of the meeting of the board of directors (including the bidding advertisement if there is to be bidding used and the legal public notice); (2) (a) a Notice of the Issue Terms and Determination of the Lowest Bid Price,\textsuperscript{117} (b) related reference materials and a Written Computation of the Lowest Bid Price\textsuperscript{118} in the case of the bidding system; (3) a press release as to determination of the issue price of the new shares for public subscription and, in the case of book building, the tentative terms of such price; (4) a writing In re

\textsuperscript{113} 監査概要書.
\textsuperscript{114} 取締役会議事録.
\textsuperscript{115} 公開予定書.
\textsuperscript{116} 要約仮目論見書.
\textsuperscript{117} 発行条件及び入札の下限価格決定通知書.
\textsuperscript{118} 入札の下限価格算定書.
the Affairs of the Bidding119 when the bidding system is being used; (5) a press release as to the terms of issue of the new shares and the minimum price to be determined by bidding in such case; and (6) a public table of materials concerning the terms of issue where book building is involved.

D – 22
Conclusion of the underwriting contract with the underwriting securities companies.

D – 21
Filing of the first Corrected Valuable Securities Statement with the Finance Bureau accompanied by a Corrected Preliminary Provisional Prospectus.120 A Summary of the Bidding,121 a Written Notice of Conduct of Bidding,122 and the Bid Proposal Intermediary Writing123 are to be included when bidding is used. Moreover, publication of a notice of the resolution to issue new shares, an advertisement for the submission of bids and notice of the Intermediary Writing (this last by the Japan Over-the-Counter Securities Company) are also to be done in the case of bidding.

D – 17
The Corrected Valuable Securities Statement becomes effective.

D – 17
Proposal of the bidding date (the day upon which the bidding will occur).

or

D – 16
Bidding date if there is to be bidding. Submission of a Written Notice of Determination of the Public Offering Price,124 a press release regarding the price determined for a capital increase/public subscription, etc. and materials related to the determination of this price.

D – 11
Filing of the second Corrected Valuable Securities Statement with the Finance Bureau. Submission of the Roll of Successful Bidders125 and Detailed Table of Successful Bid Results126 upon bidding.

D – 9
The second Corrected Valuable Securities Statement becomes effective.

D – 7
Period for subscribing to the new shares.

through

D – 6

D – 6
Presentation of the Corrected Prospectus to the applicant securities companies.

D – 4
Submission of the Report of Public Subscription/Capital Increase, Etc.127

D – 1
Paying-in date.

D
Registration date, date of commencement of sales and date of the increase of capital. Submission of a Report of Conduct of the Public Offering of Shares of Stock,128 and delivery to the registration applicant company by JASDA of a Certificate of Registration129 and a Written Notice of Registration130

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119. 入札実務について.
120. 仮正要約仮目論見書.
121. 入札要領.
122. 入札実施通知書.
123. 入札申込取消書.
124. 公開価格決定通知書.
125. 落札者名簿.
126. 落札結果明細表.
127. 公募増資等の実施報告書.
128. 株式の公開実施報告書.
129. 登録証.
130. 登録通知書.
V. DOCUMENTS TO BE PREPARED BY THE REGISTRATION APPLICANT COMPANY

The registration applicant company must provide very detailed information about itself in regard to the following matters in the Report for the Purpose of the Registration Application\textsuperscript{131} to be filed together with the Registered Issue Registration Application:

1. The reasons for applying for the registration.
2. History of the company.
3. Transition in business operations over the past ten years.
4. Officers and large shareholders.
5. Status of labor affairs.
7. Position held in the industry.
9. Substance of the business.
11. Personally related and capital related companies.
13. Other matters.

The following documents should be attached to the Report for the Purpose of the Registration Application.\textsuperscript{132}

1. Copies of minutes of shareholders meetings, board of directors meetings, and board of auditors meetings held after the commencement of the business year containing the application date that affect any item in 1 through 13 above.
3. Copies of closing reports (materials submitted to the ordinary general shareholders meeting under the Commercial Code\textsuperscript{133}) and final juridical persons tax returns with schedules for all business years within the past three calendar years prior to the year of the application date (the same for merging companies if there was a merger during this period).
4. Catalogs and pamphlets for manufactured goods and merchandise.

\textsuperscript{131} In re Changes in the Form of Documents Required to Be Submitted Upon Application for Registration 登録申請際し提出を要する書類の様式の変更について, JASDA 日証協 (OTC Review Department 店審) Notice 6 No. 334, March 16, 1993, 1; In re Changes, Etc. in the Form of Documents Required to Be Submitted Upon Application for Registration 登録申請際し提出を要する書類の様式の変更等について, JASDA 日証協 (OTC Review Department 店審) Notice 7 No. 881, Dec. 25, 1995; JASDA OTC HANDBOOK 120–47.

\textsuperscript{132} JASDA OTC HANDBOOK 79, 146–47.

\textsuperscript{133} COM C art. 283.
5. Copies of the Charters as well as closing reports and final juridical persons tax returns with schedules during the past three years for specified related companies.\textsuperscript{134}

6. Copies of the Audit Summaries for specified related companies (excluding subsidiaries included in consolidated statements) for the most recent completed business year.

7. Copies of the closing reports for capital related and personally related companies (other than specified related companies) during the past three years.\textsuperscript{135}

The Valuable Securities Report for the Purpose of the Registration Application for the business year immediately prior to the year of the application date, to be included with the Registered Issue Registration Application, must contain the following information: \textsuperscript{136}

1. General information concerning the contact point at and the location of the registration applicant company.
2. Date concerning the new offering.
3. Outline of the company.
4. Outline of the business.
5. Status of business operations.
7. Accounting situation.
8. Circumstances of a business group (i.e. parent and subsidiary companies).
10. Other information to be considered.

Other documents which must be either prepared or obtained and furnished by the registration applicant company to the applicant securities companies for submission to JASDA on the application date in connection with the Registered Issue Written Registration Application are: \textsuperscript{137}

1. A written oath\textsuperscript{138} by the registration applicant company that all documents submitted in accordance with JASDA Fair Prac. Reg. 2 and Fair Prac. Reg. 2 Det. Rules are the truth and contain no omissions.\textsuperscript{139}

2. A written compact\textsuperscript{140} by the registration applicant company that it will do the following: \textsuperscript{141}

\textsuperscript{134} See page 37 infra.
\textsuperscript{135} See pages 12 and 13 supra.
\textsuperscript{136} Fair Prac. Reg. 2 Det. Rules art. 2 (1), Sep. Sch. 1 (1)(ii); Disclosure Min. O. art. 8 (2), Form No. 2-4.
\textsuperscript{137} Fair Prac. Reg. 2, art. 3; Fair Prac. Reg 2 Det. Rules art. 2 (1), Sep. Sch. 1 (1); JASDA OTC HANDBOOK 78-79.
\textsuperscript{138} 請知識語
\textsuperscript{139} Fair Prac. Reg. 2 Det. Rules art. 2 (2).
\textsuperscript{140} 請約語
\textsuperscript{141} Fair Prac. Reg. 2, art. 3 (2).
a. Remain fully conscious of the significance of the public offering of its shares as a registered issue and keep in mind the protection of the investor.
b. Comply with demands made by the applicant securities companies founded upon the rules and demands of JASDA.
c. Carefully obey the regulations prescribed by JASDA regarding valuable securities to be sold over-the-counter.
d. Respond to a seeking to hear about circumstances and a request for the collection of materials by JASDA.
e. Strictly and scrupulously contact the applicant securities companies and JASDA concerning company information involving serious matters that must be reported by the applicant securities companies to JASDA under Fair Prac. Reg. 2.142
f. Other matters perceived by JASDA as being separately necessary for basic rule issues or special rule issues.

3. The Charter of the registration applicant company.
4. Copies of a Half Term Report for the Purpose of the Registration Application and an Interim Audit Report for the interim accounting period of the prior business year.145
5. Audit Summaries prepared by the outside accountants for JASDA concerning those audits of the registration applicant company that are attached to the Valuable Securities Report for the Purpose of the Registration Application or that concern the Audit Report in 4 above.146
6. Formal business reports of the registration applicant company for its most recent three business years.
7. A Detailed Schedule of Payments relating to expenses incurred in the course of turning a business in a new field into an operating business enterprise (when application is being made for a special rule issue).
8. A sample of the certificate of the stock for which the registration is being sought.
9. A certified extract copy of the government's company recording book regarding the registration applicant company.
10. An Outline of the Company, pamphlets concerning products and other reference materials introducing the registration applicant company.
11. Copies of a Half Term Report for the Purpose of the Registration Application and an Interim Audit Report covering the beginning of the

142. Fair Prac. Reg. 2, art. 30 (1).
143. 登録申請のための半期報告書.
144. 中間監査報告書.
145. See Disclosure Min. O. art. 18, Form No. 5, which provides the model for the Half Term Report, and Securities Exchange Law art. 139-2 dealing with the Interim Audit Report.
147. 営業報告書.
148. 支出明細書.
current business year must also be filed if the registration takes place more than nine months after the close of the prior business year.

12. The Written Compact Concerning the Continuing Holding and Deposit of Shares of Stock and either certificates pertaining to the protective deposit or certificates of custody.

13. A Memorandum Concerning the Continuing Holding and Deposit of Success Compensation Type Warrants (including minutes of the board of directors meeting awarding the warrants as compensation, salary or a bonus and documents in evidence of the award).

14. Minutes of meetings of the board of directors of the registration applicant company regarding special resolutions of a general meeting of shareholders setting the conditions for the award of a right to accept new shares to an officer or employee.

15. The contract with a stock affairs representative agency.

16. Audit contract(s).

17. A list of persons with a specially-related interest (in the standard kana order which is equivalent to alphabetic order in English).

18. Monthly statements computing profit and loss for the business year prior to that of the application date and for the time of the application comparing budgeted figures with actual results.

19. A Statement as to the Responsible Officer for Disclosure of Information.

20. Consent to share certificate custody and transfer activities.

21. Copies of the following documents if they were required to be submitted to the Ministry of Finance:
   a. Public Offering Sale Statement (including corrected copies here and in c and d below).

The registration applicant company must submit copies of regular Audit Reports prepared by a certified public accountant or audit juridical person qualified in Japan reviewing the applicant’s final financial statements (consolidated or unconsolidated balance sheets and profit-and-less statements as applicable, consolidated computation of surplus statements and computations of the disposition of profit or disposal of loss) for the past two business years prior to the year of the

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149. 株式の継続保有及び預託に関する契約書。
150. 成功報酬型ワランツの継続保有及び預託に関する覚書。
151. COM C arts. 280-19 (2), 343.
152. See pages 12-13 supra.
153. See pages 12-13 supra.
155. 公開買付届出書。
156. 公開買付撤回届出書。
157. 公開買付報告書。
158. 意見表明報告書。
application date. JASDA may seek such other further data and reports as it deems necessary in connection with the application.

Finally, the following documents are to be submitted to JASDA by the registration applicant company following authorization by the Board of Governors of JASDA, but before registration:

1. Consent to the Representative Applicant Member Statement in which the registration applicant company agrees to the selection of the representative applicant member by the managing securities companies made in the Representative Applicant Member Statement and Consent filed in behalf of the securities companies.
2. Copies of the first formal resolution of the board of directors to seek public subscription for or sale of new shares without specifying terms, the second formal resolution of the board of directors to seek public subscription for or sale of new shares including the terms thereof and notices and news releases involving these resolutions.
3. Copies of the Valuable Securities Statement or Valuable Securities Notice, required attached documents and a Preliminary Provisional Prospectus.
6. A copy of the Notice of the Statement Becoming Effective.
7. One copy each of the underwriting contracts.
8. A copy of the Schedule for Public Offering of Shares of Stock.
10. A copy of the Report of Conduct of the Public Subscription/Capital Increase, Etc. as a speedy report.
11. Samples of new share certificates.
12. A certified extract copy of the government’s company recording book regarding the registration applicant company after it has been revised.
14. Materials furnished to the newspaper reporters club on the date of commencement of sales.
15. The documents mentioned in item 21 on page 30 above and a Half Term Report for the Purpose of the Registration Application and Interim Audit Report covering the beginning of the current business year must be filed at this time if they cannot be submitted until after the authorization of the registration.

161. Fair Prac. Reg. 2 Det. art. 2 (1), Sep. Sch. 1 (2); JASDA OTC HANDBOOK 80.
162. 代表申請会員届出同意書.
163. 代表申請会員届出並びに同意書.
164. 有価証券通知書.
In addition, the following documents are to be presented depending upon whether bidding or book building was used to produce the initial offering price:

1. Bidding
   a. A copy of the Written Computation of the Minimum Bid Price and reference in regard thereto.
   b. A copy of the Guide to Affairs Concerning the Bidding.
   c. A copy of the notice to registration applicant company personnel regarding self-restraint in participation in the bidding.
   d. A copy of the Roll of Successful Bidders.
   e. A copy of the Detailed Table of Successful Bid Results.

2. Book Building
   a. A copy of the Written Notice Concerning a Summary of the Make-Up of the Consignment Sale Group.
   b. One copy each of the Tables of Materials Involved in Deciding the Issuance Terms.
   c. One copy each of materials concerning computation of the public subscription/capital increase price.

The dates for the submission of most of these documents will be found on pages 24–26 above.

VI. CHANGES REQUIRED TO BE MADE IN THE REGISTRATION APPLICANT COMPANY BEFORE APPLYING FOR REGISTRATION

A. Management Controls

The project team (particularly with the assistance of its lawyer and accountant members) should carefully examine the registration applicant company to see that a complete and firm set of management controls are in place.

JASDA stresses that in order to protect the investor these controls must provide a structure appropriate to the scale of the business in its industry modeled on that of other companies similarly situated in the industry which have recently gone public. These controls should move the company away from an individualistic style of management into an organized structure of business operations in such a way as to assure that the company is in full compliance with laws, orders and the rules of JASDA and to prevent the occurrence of improprieties and troubles.

B. Rules

An adequate set of internal rules must be established (present provisions being changed to the extent necessary in preparation for going public), maintained and work smoothly with business being conducted effectively and efficiently within the

165. JASDA OTC HANDBOOK 80–81.
registration applicant company before the end of the business year immediately prior to the application date.

The company's Charter should be amended if necessary to provide that public notice will be given in a nationally circulated newspaper published daily rather than the Kanpō (Official Gazette) published by the government. Changes should also be adopted to permit the appointment of a title transfer agent, set the unit for par value shares at 50,000 yen if par is less than 50,000 yen, remove any restrictions on the assignability of shares, provide for the establishment of Stock Affairs Handling Rules, and establish a procedure for consent to a share certificate, etc. custody and transfer system.

The company must in particular establish and maintain at least the following rules and regulations:

1. Basic Rules
   b. Executive Committee Rules.
   c. Regulations of the Board of Directors.
   d. Rules of the Board of Auditors.
   e. Stock Affairs Handling Rules.

2. Rules Related to Business Organization
   a. Occupational Authority Rules.
   b. Occupational Division of Duties Rules.
   c. Rules Relating to Related Company Controls.
   d. Organization Rules.
   e. Staff Coordination Rules.

3. Rules Relating to Personnel
   a. Employment Service Regulations.
   b. Officer Severance Payments in Recognition of Service Rules.

4. Rules Relating to Affairs
   a. Accounting Rules.
   b. Budgetary Control Rules.
   c. Claims Control Rules.
   d. Cost Accounting Rules.
   e. Fixed Assets Control Rules.
   f. Internal Audit Rules.
   g. Purchases Control Rules.
   h. Sales Control Rules.

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166. 報告
168. Ringi 条例
169. Commonly called “Work Rules” in English.
5. Other Rules
   c. Employee Stock Holding Rules.
   d. Insider Transaction Rules.
   e. Rules for the Control of Orders Placed on Outsiders (if numerous).
   f. Rules for the Administration of Rules.
   g. Valuable Securities Operating Rules (if securities are continuously being handled).

C. Accounting Organization

The accounting organization of the company should be carefully studied. There should be a full audit for the prior two business years before the application date. There should also be financial statements for the prior five business years before the year of the application date to which the Japanese Principles of Business Accounting and Financial Statement Regulations were applied. Moreover, there must be a special audit for the purpose of the registration application, undertaken jointly by two or more certified public accountants or an audit juridical person, applying the rules of the Securities Exchange Law governing a special audit prior to the listing of stock on a securities exchange.

The following questions are to be asked and a system established that permits them to be answered most affirmatively:

1. Starting with the cost accounting system, is the company's entire accounting system operating effectively?
2. Are the accounting rules adopted by the company complete and do they apply Japanese generally recognized standards of fairness and propriety?
3. Is the accounting organization controlled and managed effectively pursuant to an appropriate structure of internal checks?
4. Are the methods used to handle accounting fair and proper viewed in terms of Japanese practice?

Going public requires the company to be able to disclose profits promptly to its shareholders and investors. Therefore, systems of monthly closings, budgetary controls, conduct of business in accordance with mid- and long-term plans, analysis of differences between computations on a monthly base and actual results, and the ability to take profit forecasts and planning into account must be in place before the beginning of the business year prior to that of the application date. Normally this will require utilization of an effective internal Electronic Data Processing (EDP) system.

D. Internal Controls

JASDA defines "internal controls" in the broad sense as systems, organization, methods and procedures established by the operator of a business in order to preserve the assets of the enterprise, assure the trustworthiness and correctness of accounting records, and comprehensively plan, adjust, and judge the effectiveness of the activities carried on in operating the business. The three basic elements of systemization, qualified personnel and the maintenance of adequate records must be in place. Key points for study are: the existence of clear distinctions in such matters as company organization and the division of tasks, the presence of a full body of adequate rules, the determination of policy involved in business operating plans, the implementation of profit planning and the conduct of budgetary control for at least one prior business year, and continuing internal audit on both a regular and irregular basis.

"Internal controls" in the narrow sense are said to be founded upon the two pillars of internal checks and an internal audit system.

Internal checks involve a system for managing the affairs of a business designed to identify improprieties and error as a consequence of the working of mutual checks in daily operations between persons and departments under a clear distinguishing of professional tasks. Therefore, the company must eliminate inconsistencies arising from the mutual overlapping of tasks and rectify its Organization Rules, Occupational Division of Duties Rules and Occupational Authority Rules so that the tasks to be performed are clear and internal checks can work effectively.

Both periodic and irregular internal audit of such places as the head office, plants and branch offices should be conducted in order to verify that there are staff members with distinct and different responsibilities immediately under the president of the company, that departments with different and distinct areas of specialization have been established, that such activities as accounting and sales are being performed in accordance with laws, orders and the rules of JASDA and that business operations are effective.

One person should be named within the company with the sole responsibility for internal audit. A written internal audit plan should be prepared and put in force with regular internal audit reports to the president and the regular enforcement of recommendations for improvement of operations. This system should be in effective operation by the end of the business year prior to that of the application date and be confirmed by the applicant securities companies.

E. Stock Handling

Upon registration the handling of all stock and shareholder affairs must be passed to a stock transfer agent selected from among firms designated by JASDA. Therefore, in the interim, during which preparations are being made for the registration, all such matters should be delegated to a stock affairs representative agency and removed from the tasks of the company's staff.172

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172. See 15 on page 30 regarding the submission of the contract with this agency.
Related Companies

Capital related and personally related companies of the registration applicant company should be carefully scrutinized since their position will be thoroughly reviewed by the applicant securities companies. It is desired that any problems in the relationship be corrected by the beginning of the business year prior to the year of the application date.

If the related company is involved in the manipulation of the profits or price of the stock of the registration applicant company, measures will be required to have it eliminate all possibility of control by merger with or becoming a 100 percent subsidiary of the registration applicant company, assignment of the ownership of its stock or its business to a third party, eliminating the problem transactions or its dissolution.

The following questions will be specifically considered upon review by the applicant securities companies:

1. Is the content of transactions with the related company open and fair?
2. Is there no manipulation of profit through the related company and no risk that it could occur?
3. If the related company is in the red or has excessive debt, is there a prospect of changing this situation?
4. Are the remuneration and bonuses proper for directors serving concurrently as such in both companies?
5. Do the officers of the registration applicant company own shares of stock in the related company (except where there are no transactions between both companies and neither transactions nor a competitive relationship will arise between these companies in the future)?
6. Does the related company own any of the shares of stock of the registration applicant company (excluding where it is a parent company or a property holding company)?

In particular, the review by the applicant securities companies will consider the need for the continued existence of the related company, adjusting transactional and other influential relationships, adjusting dual service by officers in both the registration applicant company and related companies as well as transactional relationships with such officers, and taking a careful look at the profit base in the registration applicant company as a single enterprise.

If the presence of the related company is lawful and reasonable from a business standpoint and its existence is important for the applicant company, the companies will normally be required to prepare consolidated financial statements. If its existence is not important, separate financial statements of the related company must be submitted. JASDA requires the submission of the closing reports of personally related and capital related companies for the past three years.  

173. See 7 on page 28 supra.
A third form of related company is a "specified related company" governed by similar rules. This term covers companies coming under either one of the following cases: 174

1. The case where either the registration applicant company or another company owns 175 20 percent or more of the voting rights of a third company and the registration applicant company and the other company on their side have a relationship with the third company coming under either a or b below:
   a. A relationship where revenues (or expenses) derived from transactions with the third company are 20 percent or more of total revenues (or total expenses).
   b. A relationship where the total of claims and debts derived from transactions with the third company within assets and liabilities on the balance sheet amounts to 10 percent or more of total assets.
2. The case where two or more third companies participate in transactions of less than 20 percent each under 1a above with the registration applicant company, but the total of each of the separate figures for each of these companies comes to 20 percent or more, and the registration applicant company has the voting rights relationship specified in 1 above plus transactions with the third companies constituting 10 percent or more of its total revenues (or expenses).

JASDA requires submission of the financial statements of a specified related company for the most recent past three years, its Audit Report by a Certified Public Accountant for the immediate prior business year and other Audit Reports for the other two years among the past three years, its closing reports and final tax returns for the past three years, and a copy of its Charter. A registration applicant company is required to be independent from its related companies in such areas as common officers and employees, transactions and control.

It is desirable that officers (directors and statutory auditors) and employees of the registration applicant company be persons who are working full time in the company in Japan. Therefore, except within specified parameters, it will be necessary to eliminate officers who are serving at the same time in this same capacity in a parent company or another company in a senior position as to capital and persons sent out from a related company to work on detached service.

Specifically, the requirements imposed by JASDA are:

1. Officers serving jointly in the registration applicant company and another related company will be permitted if they are not full-time officers of the registration applicant company and their number does not exceed that of those who are full-time officers. Accordingly, it will be required that a

174. JASDA OTC HANDBOOK 7; see also Valuable Securities Listing Rules 有価証券上場規程, Tokyo Exchange Rule established April 1, 1949, art. 3 (2) (v).
175. Shares owned by officers of these companies or through third parties in behalf of the officer are deemed to be owned by the company. JASDA HANDBOOK 8.
176. See page 28 supra.
quorum of the board of directors be full-time directors resident in Japan. Also, where there are two statutory auditors at least one must be full time.

2. It is considered highly undesirable that staff personnel in top positions at the head of the registration applicant company or its departments be persons sent out on detached service from the parent company, etc. Therefore, in principle, elimination of persons holding these posts on detached service is required. However, where it can be shown in some cases that such a staff position is unavoidable for the time being for proper reasons, this service will be permitted a year or two after registration provided that it can be confirmed by JASDA that it is certain that the practice will cease after this time.

Transactions with related companies, involving such matters as purchases or sales, lease of immovable property and the guaranty of debt, must be appropriate and subject to objective conditions with the terms not being influenced by the interests of the related company.

Except where it is a property holding company, a parent company must join the registration applicant company in being a “public company” (disclosure company) under Japanese law. Of course, if it is judged on careful scrutiny that there are no important transactions with the parent company which affect the major operations of the registration applicant company and there are not any problems as to the latter’s independence, no special issues will arise. But, if major transactions do take place between these companies, then an additional standard must be met by the parent company. A Japanese parent company meets this standard if its stock is listed on a Japanese securities exchange or traded on the over-the-counter market or it qualifies as a “continuous disclosure company.”

A foreign company meets the standard if it continually submits its financial statements, etc. that have been subjected to audit certification by an auditor as either meeting or exceeding a specified standard fixed by the law of the foreign company’s country, it is under the duty to permit these statements, etc. to be examined by the public and JASDA can also examine all disclosure materials of these financial statements. Under these circumstances the parent company, etc. will be treated as a “public company” in Japan.

The Japanese Commercial Code permits the board of directors of a company to authorize a director to engage in a transaction either with or in competition with the company. But as transactions of this sort pose the possibility of an adverse effect on a registration applicant company and raise problems in the protection of its investors, the applicant securities companies will upon review require either that they be eliminated or changed into a proper form of transaction.

177. 繰続開示会社. See Disclosure Min. O. art. 1 (xxviii).
178. CoM C art. 265.
VII. REVIEW BY THE APPLICANT SECURITIES COMPANIES

A. Registration Review

Review by the securities companies performs the same role as the substantive review by a securities exchange when listing on an exchange is sought. The standards applied at this time are not only the minimum formal standards described as the grounds for eligibility alone, but also the substantive standards developed by JASDA as a prerequisite for listing. This review can be quite a stringent process. Although it is still not as strenuous as the review conducted by securities exchanges, new requirements imposed by JASDA over the past decade modeled on those required for listing on an exchange, have brought it much closer to the same process. The results of the review are recorded in a Registration Applicant Company Written Investigation and Report of Review which together constitute the basis for JASDA deciding whether to grant the application.

All of the matters dealt with in the Report for the Purpose of the Registration Application, the Valuable Securities Report for the Purpose of the Registration Application, the Half Period Report for the Purpose of the Registration Application (used to review seasonal changes) and the Audit Summaries will be carefully checked and reviewed by the applicant securities companies in connection with the Valuable Securities Statement to be filed with the competent Finance Bureau of the Ministry of Finance under the Securities Exchange Law.

In particular, the subjects of special study will be:

1. The direction of business operations and trends in the company's particular features and business results.
2. Compliance with the rules of Japanese law (especially company law and laws governing the industry) and with standard practices in the industry.
3. Maintenance of required company documents in a proper form.
4. The situation of its managers and employees.
5. The situation of large shareholders and related companies as well as transactional relationships with them.
6. The financial state of capital related and personally related companies and the results of their business operations.
7. The substance of the business and the state of disclosure of its internal operations.
8. The profit plan.
11. State of audit conducted by the statutory auditors.
12. Management of receivables, inventories and fixed assets.
13. Matters having the possibility of a major influence on the judgment of investors concerning the degree of risk in investment in the registration applicant company.

179. See Section II and III supra.
14. Matters regarding third party allocated capital increases and assignment or receipt of assignment of shares by persons with a specially-related interest, etc.
15. Matters regarding cases in litigation, environmental injury problems, etc.
16. Principal questions from other applicant securities companies and answers thereto.
17. Other matters especially deserving investigation.

Other items to be checked are covered above in connection with the documents to be prepared by the registration applicant company (described in Section V above) and the changes required to be made. Based on this review, the responsible persons in the Underwriting Division or Review Division of the applicant securities companies will make a final determination whether to go forward with the application for registration.

B. Underwriting Review

Securities companies underwriting a stock issue must consider some of the above matters in greater depth as well as some other issues. They shall examine whether the company issuing the stock is likely to meet the future expectations of its investors and, if it is suitably gathering capital from capital markets. They shall also take into account the results of an investigation by security analysts. The underwriting securities companies are required to review strictly and confirm the following matters and then make a decision as to whether they should go ahead and underwrite based upon a comprehensive judgment respecting all factors including any and all data obtained as needed on request to the auditors:

1. Financial state and business results.
2. Use of funds obtained and the results.
3. State of distribution of profits and thinking about such distribution.
4. Quantity of shares, etc. issued and the issue price.
5. Circulation and profitability of shares.
6. State of shares, etc. issued in the past.
7. Direction of movement in the price of shares.
8. Other matters regarded to be necessary by the securities companies.

VIII. DISCLOSURE REQUIREMENTS

A. In General

Japanese securities law, created during the post World War II occupation by the United States occupation authorities based on US securities law, has always required an extensive disclosure of information to the public regarding the activities

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180. See Section VI, supra.
181. Underwriting Rules art. 6.
of a company whose stock is publicly traded. But the scandals of the late 1980s brought on the imposition of even more extensive requirements.

The reports, statements and other information that must be furnished in connection with the Registration Application have been listed. The registration applicant company will also be required, at the behest of the representative securities company, to specify an officer in charge of disclosure of information and a staff member responsible for business contacts with JASDA and report these names and all changes therein without delay to the latter on a prescribed form. The officer must be a representative director or a person selected by him. The officer shall be available for consultation on disclosure matters, handle contacts with organs of the media and make prompt disclosures as required by law and JASDA.

"Organs of the media" are defined to mean: (1) newspaper companies engaged in the business of selling a newspaper published daily that comprehensively reports current events within Japan; (2) news services comprehensively supplying matters relating to current events to the newspaper companies of (1); (3) newspaper companies engaged in the business of selling a newspaper published daily that completely reports matters concerning industry and economics in Japan; and (4) NHK and other persons generally engaged in the broadcasting business under the Broadcasting Law.

The registration applicant company and the representative securities company must consult about matters required to be disclosed before disclosure to the media. When the disclosure is made the matter shall be reported in writing by the representative securities company to JASDA and made available for inspection by the public.

B. Documents to be Filed After the Successful Registration of Securities

After the securities are successfully registered, there are a number of regular reports to be made to the Ministry of Finance and special reports JASDA whenever certain business events take place. The securities markets in Japan are licensed and supervised by the Ministry of Finance, and reports to the Ministry submitted through the competent Finance Bureau provide information on the general health of the registered companies. JASDA is concerned with business events which will affect the price of securities being traded. Thus, JASDA requires notification in the case of a serious event (called an "important fact") in the registered company's business, information about shareholders meetings, notices relating to the issuing of new shares, information regarding a merger of the company and changes in the Charter. With the exception of shareholders meetings, none of these reports will be

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182. See Section IV(C) and V, supra.
185. Securities Law Enf. O. art. 30 (1).
filed regularly by registered companies and it is possible that none of the events will occur at all.

The documents to be presented to the Ministry of Finance are as follows:

<table>
<thead>
<tr>
<th>DOCUMENT</th>
<th>TIME TO BE PRESENTED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valuable Securities Report</td>
<td>A month or less after registration.</td>
</tr>
<tr>
<td>(Form #4).</td>
<td></td>
</tr>
<tr>
<td>Valuable Securities Report</td>
<td>Three months or less after the end of each</td>
</tr>
<tr>
<td>(Form #3).</td>
<td>business year.</td>
</tr>
<tr>
<td>Half Term Report</td>
<td>Three months or less after the end of each</td>
</tr>
<tr>
<td>(Form #5).</td>
<td>business year.</td>
</tr>
<tr>
<td>Extraordinary Report.</td>
<td>Immediately after the event occurs.</td>
</tr>
<tr>
<td>Valuable Securities Statement</td>
<td>Up to thirty days before the sale.</td>
</tr>
<tr>
<td>(Form #2).</td>
<td></td>
</tr>
</tbody>
</table>

The reports and additional documents required by law and JASDA are detailed and thorough. The following is a list of the reports for JASDA and the media, and the documents required in the case of shareholders meetings, the issue of new shares under certain circumstances and the happening of an important fact affecting the business. All companies affected, their officers, prescribed personnel and others having a specified connection with the company are required to see that all the listed events are reported both to two organs of the media and JASDA before any transfer of stock may take place.

<table>
<thead>
<tr>
<th>DOCUMENT</th>
<th>TIME TO BE PRESENTED</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Regular General Reports Regarding:</td>
<td></td>
</tr>
<tr>
<td>1. Regular shareholders meetings</td>
<td></td>
</tr>
<tr>
<td>(1) Notice of the resolutions of the board</td>
<td>Immediately after the decision.</td>
</tr>
<tr>
<td>of directors concerning the closing of the</td>
<td></td>
</tr>
<tr>
<td>books (1 copy).</td>
<td></td>
</tr>
<tr>
<td>(2) Brief account of the regular or</td>
<td>Day of the board of directors</td>
</tr>
<tr>
<td>consolidated closing of the books</td>
<td>meeting closing the books.</td>
</tr>
<tr>
<td>(6 copies).</td>
<td>Before or when they are sent to the shareholders.</td>
</tr>
<tr>
<td>(3) Sample of notice calling a shareholders</td>
<td></td>
</tr>
<tr>
<td>meeting (2 copies).</td>
<td>Before or when they are sent to the shareholders.</td>
</tr>
<tr>
<td>(4) Sample of notice of resolutions to be</td>
<td></td>
</tr>
<tr>
<td>considered at a shareholders meeting (2</td>
<td></td>
</tr>
<tr>
<td>copies).</td>
<td></td>
</tr>
<tr>
<td>(5) Annual Business and Operations Reports</td>
<td></td>
</tr>
<tr>
<td>(2 copies).</td>
<td></td>
</tr>
<tr>
<td>(6) Press releases (6 copies).</td>
<td></td>
</tr>
<tr>
<td>(7) Copies of the Valuable Securities Report</td>
<td></td>
</tr>
<tr>
<td>(including copies of Corrected Reports)</td>
<td></td>
</tr>
<tr>
<td>and attachments (2 copies).</td>
<td></td>
</tr>
<tr>
<td>(8) Charter (2 copies).</td>
<td></td>
</tr>
</tbody>
</table>

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188. 寄時報告書.
2. Special shareholders meetings.
   (1) Notice of the resolution of the board calling the meeting (1 copy).
   (2) Schedule relating to the term used for determining shareholders rights or the base date (1 copy).
   (3) Sample of the notice calling the shareholders meeting (2 copies).
   (4) Sample of the notice of resolutions to be considered at the shareholders meeting (2 copies).

3. Interim closing of the books.
   (1) Notice of the resolution of the board of directors determining the interim closing (submitted only by a company not submitting (2) below (1 copy)).
   (2) Brief account of the interim closing of the books (6 copies).
   (3) Notice concerning closing the shareholders name book for interim dividends.
   (4) Notice concerning the base date for interim dividends (1 copy).
   (5) Copies of the notice of the resolution to declare interim dividends (2 copies).
   (6) Interim Business and Operations Reports (2 copies).
   (7) Press releases (3 copies).

4. Change in the company’s name.
   (1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).
   (2) Schedule (3 copies).
   (3) Materials relating to the shareholders meeting.
   (4) Press release (3 copies).
   (5) Application for recording the change (1 copy).
   (6) Charter after the change (2 copies).
   (7) Sample share certificates (1 copy of each different class).
   (8) Copies of the Stock Affairs Handling Rules after amendment (2 copies).
   (9) Extract of the company’s recording after the change (1 copy).

5. Change in the objects or newspaper of publication of the company.
   (1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).

   Immediately after the decision.
   Immediately after the decision.
   Immediately after the decision.
   Before or when they are sent to the shareholders.
   Before or when they are sent to the shareholders.

   Immediately after the decision.

   Immediately after the decision.
   Immediately after the decision.
   Immediately after they are prepared.
   Immediately after they are prepared.
   Immediately after they are prepared.
   Immediately after they are prepared.
   Immediately after they are prepared.
   Immediately after the recording.

   Immediately after the decision.
6. Change in the site of the head office of the company.
   (1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).
   (2) Notice of a change of the site of the head office (2 copies).
   (3) Materials relating to the shareholders meeting. (2 copies to each one).
   (4) Press release (3 copies).
   (5) Charter after the change (2 copies).
   (6) Extract of the company's recording after the change. (1 copy).
   (7) Sample share certificates (1 copy of each different class).
   (8) Other documents to be sent to shareholders (2 copies to each one).

7. Change in the officer in charge of disclosure of information or the person responsible for business contacts with JASDA.
   (1) Statement of the change (1 copy each).

8. Determination or change of a transfer agent.
   (1) Notice of the resolution of the board calling a shareholder meeting (1 copy).
   (2) Materials relating to the shareholder meeting (2 copies to each one).
   (3) Copy of the contract entrusting the handling of stock affairs and supplementary materials certified by the representative (1 copy).
   (4) Notice to the shareholders (2 copies).
   (5) Press release (3 copies).
   (6) Charter after the change (2 copies).
   (7) Stock Affairs Handling Rules after the change (2 copies).
   (8) Extract of the company's recording after the change (1 copy).
   (9) Sample of new share certificates (1 copy of each different class).

9. Change in the time of the closing of the books.
   (1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).
   (2) Materials relating to the shareholders meeting. (2 copies to each one).
   (3) Press release (3 copies).
   (4) Charter after the change (2 copies).

10. Conversion of par shares to no par shares or no par shares to par shares.
    (1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).
    (2) Schedule (3 copies).
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(3) Materials relating to the shareholders meeting (2 copies to each one).

(4) Press release (3 copies).

(5) Application for recording the change (1 copy).

(6) Charter after the change (2 copies).

(7) Sample share certificates (1 copy of each class).

11. Change in the class of shares.

(1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).

(2) Schedule (3 copies).

(3) Materials relating to the shareholders meeting (2 copies to each one).

(4) Press release (3 copies).

(5) Application for recording the change (1 copy).

(6) Charter after the change (2 copies).

(7) Sample of the new share certificates (1 copy of each class).

12. Change in the number of shares that may be issued by the company.

(1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).

(2) Materials relating to the shareholders meeting (2 copies to each one).

(3) Press release (3 copies).

(4) Charter after the change (2 copies).

13. Change in the number of shares in one unit.

(1) Notice of the resolution of the board of directors calling a meeting (1 copy).

(2) Materials relating to the shareholders meeting (2 copies to each one).

(3) Press release (3 copies).

(4) Charter after the change (2 copies).

14. Other amendments of the Charter.

(1) Notice of the resolution of the board of directors calling a shareholders meeting (1 copy).

(2) Materials relating to the shareholders meeting (2 copies to each one).

(3) Press release (3 copies).

(4) Charter after the change (2 copies).

15. Change in the Stock Affairs Handling Rules or other important rules, etc. of the company.

(1) Notice of the resolution of the board of directors (1 copy).
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(2) The Stock Affairs Handling Rules, etc after the change (2 copies).

16. Change in a Representative.
   (1) Notice of the resolution of the board of directors (1 copy).
   (2) Copies of the Extraordinary Report (2 copies).
   (3) Face photograph of the new representative (1 copy).
   (4) Samples of the new share certificates (1 copy of each class).

17. Change in shares, etc. with a share certificate and the issuance of a new class of share certificate.
   (1) Sample of the new share certificates (1 copy of each different class).

18. Change of certified public accountants, etc.
   (1) Notice of the change.

19. Other reports specially sought by JASDA.
   (1) The report in writing.

IX. REPORT OF MATTERS FOUNDED UPON AN IMPORTANT FACT CONCERNING BUSINESS OPERATIONS, ETC.

All actions shall be accompanied by a press release, three copies of which should be provided. Items marked with an asterisk need not be reported if it is recognized by JASDA, on consultation, that the influence of the fact on the investment judgment of an investor would be de minimus.

A. Reports Concerning Matters Decided

1. The issue or sale of shares and the issue of convertible debentures.

   a. Capital increase by public subscription.

   DOCUMENTS
   (1) Notice of the resolution of the board of directors (1 copy).
   (2) Schedule for issuing new shares (3 copies).
   (3) Copies of the Valuable Securities Statement or Valuable Securities Notice (including copies of changes and attached documents) (2 copies).
   (4) Prospectus (including a Corrected Prospectus) (2 copies).

   TIME
   Immediately after it is prepared.
   Immediately after the decision.
   Immediately after submission to the regional Finance Bureau of the Ministry of Finance.
   Immediately after the change.
   Immediately after they are prepared.

   When the new share certificates are sent to the shareholders.

   Immediately after the change.

   Immediately after the contact on behalf of JASDA.

   Immediately after the decision.
   Immediately after the decision.
   Immediately after submission to the regional Finance Bureau of the Ministry of Finance.
   Immediately after its preparation.
(5) List of persons connected with stability manipulation (2 copies).
Immediately after the decision.

(6) Notice of determination of the issue price (offering price) (2 copies).
Immediately after the decision.

(7) Reference materials to calculate the public subscription price (2 copies).
Immediately after the decision.

(8) Application for public offering of stock (1 copy).
Immediately after submission of the Valuable Securities Statement.

(9) Copy of the notice stating that the Valuable Securities Statement is effective (1 copy).
Immediately after the notice is accepted.

(10) Sample stock subscription slip for the issue of new shares (only when remaining shares are underwritten) (1 copy).
Before or when it is sent to the shareholders.

(11) Application for changed or additional stock registration and written consent (1 copy).
Three weeks prior to the date the new shares become effective.

(12) Notice of allocation of new shares (2 copies).
At the same time as it is sent to the shareholders.

(13) Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).
Before or when the new share certificates are sent to the shareholders.

(14) Extract of the company’s recording after the change (1 copy).
Immediately after recording.

b. Capital Increase by allocating shares for value.

(1) Notice of the resolution of the board of directors (1 copy).
Immediately after the decision.

(2) Schedule for issuing new shares (3 copies).
Immediately after the decision.

(3) Copies of the Valuable Securities Statement or Valuable Securities Notice (including copies of changes and attached documents) (2 copies).
Immediately after submission to the regional Finance Bureau of the Ministry of Finance.

(4) Prospectus (including a Corrected Prospectus) (2 copies).
Immediately after its preparation.

(5) Copy of the notice stating that the Valuable Securities Statement is effective (1 copy).
Immediately after the notice is accepted.
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(6) Sample stock subscription slip (2 copies).
At the same time as it is sent to the shareholders.

(7) Notice of confirmation of the number of new shares issued (where convertible debentures are issued) (1 copy).
Immediately after the confirmation.

(8) Application for changed or additional stock registration and written consent (1 copy).
Three weeks prior to the date the new shares become effective.

(9) Notice of allocation of new shares (2 copies).
At the same time as it is sent to the shareholders.

(10) Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).
Before or when the new share certificates are sent to the shareholders.

(11) Extract of the company's recording after the change (1 copy).
Immediately after recording.

Stock split when it is done by issuing additional shares.

(1) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).
Immediately after the decision.

(2) Schedule for issuing new shares (3 copies).
Immediately after the decision.

Written summary of the state of the business.

Interim financial statements.

Audit report for the most recent two business.

(6) Anticipated balance sheet on the merger date (2 copies).
Immediately after it becomes definite.

(7) Cash flow plan schedule for six months after the merger.
Immediately after it becomes definite.

(8) Schedule of profit plan for two business years after the merger.
Immediately after it becomes definite.

(9) Written computation of the merger ratio.
Immediately after it becomes definite.

(10) Materials relating to the shareholders meeting (authorization and report) (2 copies to each one).
Before or when they are sent to the shareholders.

Immediately after submission to the regional Finance Bureau of the Ministry of Finance.
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(12) Application for changed stock registration and written consent (1 copy).

Three weeks prior to the anticipated date of the changed registration.

(13) Samples of the new share certificates (with a list of samples of the security attached) (1 copy of each different class).

Before or when the new share certificates are sent to the shareholders.

(14) Extract of the company's recording after the change (1 copy).

Immediately after recording.

d. Assigning or receiving assignment of all or part of a business.*

(1) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).

Immediately after the decision.

(2) Schedule (3 copies).

Immediately after determination.

(3) Copy of the contract (1 copy).

Immediately after it is concluded.

(4) Written summary of the assignment or receipt of assignment of a business (2 copies).

Immediately after it becomes definite.

(5) Materials relating to the shareholders meeting (authorization and report) (2 copies to each one).

Before or when they are sent to the shareholders.

e. Dissolution other than dissolution due to merger.

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

(2) Schedule (3 copies).

Immediately after determination.

f. Commercialization of a new product or new technology*

(1) Notice concerning the commercialization of a new product or new technology (1 copy).

Immediately after determination.

g. Entering into or canceling a business tie-up with another enterprise.*

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

(2) Schedule (3 copies).

Immediately after determination.
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**h. Assignment or acquisition of stock of interests pursuant to changes in a subsidiary company (see Section III above).**

1. Notice of changes in the subsidiary company or notice of the resolution of the board of directors concerning establishment of a subsidiary company (1 copy).

   Immediately after it is definite or after the decision.

2. Written summary concerning the subsidiary (2 copies).

   Immediately after it is definite or after the decision.


   Immediately after submission to the regional Finance Bureau of the Ministry of Finance.

**i. Assignment or acquisition of a fixed asset as defined by the Juridical Persons Tax Law.**

1. Notice of the resolution of the board of directors (1 copy).

   Immediately after the decision.

2. Written summary of the assignment or receipt of assignment of a fixed asset in the business (2 copies).

   Immediately after the decision.

**j. Suspension or termination of part or all of business operations.**

1. Notice of the resolution of the board of directors (1 copy).

   Immediately after the decision.

2. Schedule (3 copies).

   Immediately after determination.

**k. Petition for bankruptcy or the opening of composition or reorganization proceedings.**

1. Notice of the resolution of the board of directors.

   Immediately after the decision.

2. Schedule (3 copies).

   Immediately after determination.

3. Copies of documents concerning the petition for bankruptcy or the opening of composition or reorganization proceedings (1 copy).

   Immediately after filed with the court.

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191. See Law No. 34 of 1965, art. 2 (xxiii).
1. Opening of a new business, including commercialization of the sale of new products or the providing of a service.

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

m. Publication of an opinion or a declaration to shareholders concerning purchase of stock with voting rights, certain rights related to stock or convertible debentures other than through a securities exchange or on the OTC market (called a "public purchase").

(1) Copies of the Public Purchase Statement (including copies of a Corrected Statement and attached documents) (2 copies).

Immediately after submission to the regional Finance Bureau of the Ministry of Finance.

(2) Copies of the Statement Withdrawing A Public Purchase (2 copies).

Immediately after submission to the regional Finance Bureau of the Ministry of Finance.

(3) Copies of the Public Purchase Report (including copies of a Corrected Report and attached documents) (2 copies).

Immediately after submission to the regional Finance Bureau of the Ministry of Finance.


Immediately after submission to the regional Finance Bureau of the Ministry of Finance.

(5) Copies of a written explanation of the public purchase (including corrected copies) (2 copies).

Immediately after they are delivered.

n. Demand or petition to the Minister of Finance or JASDA involving the cancellation of registration of a valuable security traded on the OTC market.

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

(2) Reasons concerning the petition for cancellation of registration (1 copy).

Immediately after the decision.

(3) Copy of the demand for cancellation of the registration of OTC sale of a valuable security (1 copy).

Immediately after submission to the Minister of Finance.

(4) Petition for cancellation of the registration of OTC sale of a valuable security and written consent (1 copy).

Immediately after the decision.

192. Securities Exchange Law art. 27-2 (1); Securities Exchange Law Enf. O. arts. 6 (1), 7 (1); Ministerial Order Concerning the Disclosure of a Public Purchase of Share Certificates, Etc. Pursuant to a Person Who Is an Issuer Other Than a Company. 未発行者である株式の株券等の公開買付の開示に関する省令, Ministry of Finance Order No. 38 of 1990, art. 1 (vi).
### Change in the par value of shares.

<table>
<thead>
<tr>
<th></th>
<th>Description</th>
<th>Time</th>
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<tbody>
<tr>
<td>(1)</td>
<td>Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).</td>
<td>Immediately after the decision.</td>
</tr>
<tr>
<td>(2)</td>
<td>Schedule for issuing new shares (3 copies).</td>
<td>Immediately after determination.</td>
</tr>
<tr>
<td>(3)</td>
<td>Sample of the deposit certificate for share certificates submitted (2 copies).</td>
<td>When or before the deposit certificate is delivered in exchange for the share certificate receipt slip.</td>
</tr>
<tr>
<td>(4)</td>
<td>Materials relating to the shareholders meeting (2 copies to each one).</td>
<td>Before or when they are sent to the shareholders.</td>
</tr>
<tr>
<td>(5)</td>
<td>Application for changed registration and written consent (1 copy).</td>
<td>Three weeks prior to the date of the change.</td>
</tr>
<tr>
<td>(6)</td>
<td>Charter after the change (3 copies).</td>
<td>Immediately after it is prepared.</td>
</tr>
<tr>
<td>(7)</td>
<td>Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).</td>
<td>Immediately after they are prepared.</td>
</tr>
<tr>
<td>(8)</td>
<td>Extract of the company's recording after the change (1 copy).</td>
<td>Immediately after recording.</td>
</tr>
</tbody>
</table>

### Change of par shares to no par shares or vice versa.

<table>
<thead>
<tr>
<th></th>
<th>Description</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).</td>
<td>Immediately after the decision.</td>
</tr>
<tr>
<td>(2)</td>
<td>Schedule for issuing new shares (3 copies).</td>
<td>Immediately after determination.</td>
</tr>
<tr>
<td>(3)</td>
<td>Materials relating to the shareholders meeting (2 copies to each one).</td>
<td>Before or when they are sent to the shareholders.</td>
</tr>
<tr>
<td>(4)</td>
<td>Application for changed registration and written consent (1 copy).</td>
<td>Three weeks prior to the date of the change.</td>
</tr>
<tr>
<td>(5)</td>
<td>Charter after the change (3 copies).</td>
<td>Immediately after it is prepared.</td>
</tr>
<tr>
<td>(6)</td>
<td>Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).</td>
<td>Immediately after it is prepared.</td>
</tr>
</tbody>
</table>
q. Change in the class of shares.

(1) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).

Immediately after the decision.

(2) Schedule for issuing new shares (3 copies).

Immediately after determination.

(3) Materials relating to the shareholders meeting (2 copies to each one).

Before or when they are sent to the shareholders.

(4) Application for changed registration and written consent (1 copy).

Three weeks prior to the date of the change.

(5) Charter after the change (2 copies).

Immediately after it is prepared.

(6) Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).

Immediately after they are prepared.

(7) Extract of the company's recording after the change (1 copy).

Immediately after recording.

r. Change in the total number of shares of stock authorized to be issued.

(1) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).

Immediately after recording.

(2) Materials relating to the shareholders meeting (2 copies to each one).

Before or when they are sent to the shareholders.

(3) Charter after the change (2 copies).

Immediately after it is prepared.

(4) Extract of the company's recording after the change (1 copy).

Immediately after recording.

s. Change in the number of shares of stock in a unit.

(1) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).

Immediately after the decision.

(2) Schedule (3 copies)

Immediately after determination.

(3) Materials relating to the shareholders meeting (2 copies to each one).

Before or when they are sent to the shareholders.

(4) Materials to be sent to shareholders (leaflet) (3 copies).

Three weeks prior to the date of the change.

(5) Charter after the change (2 copies).

Immediately after it is prepared.
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(6) Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).

Immediately after they are prepared.

(7) Extract of the company’s recording after the change (1 copy).

Immediately after recording.

t. Newly establishing, changing or abolishing a method of preference for shareholders.

(1) Notice of the resolution of the board of directors or notice of a determination (1 copy).

Immediately after the decision or determination.

(2) Notice of the confirmed date of allocation and explanation of content (1 copy).

Immediately after the confirmation.

u. An allocation of shares or conferral of a preferred status to subscribe to shares issued by a related company granted to shareholders by a company issuing a registered issue, etc. or by the related company.

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

(2) Notice of the confirmed date of allocation and explanation of content (1 copy).

Immediately after the confirmation.

v. Conferral of a preferred status to subscribe to new shares granted shareholders by an underwriter of the new shares.

(1) Notice of the resolution of the board of directors (1 copy).

Immediately after the decision.

(2) Notice of the explanation of content (1 copy).

Immediately after the confirmation.

w. Change in a trust contract, underwriting contract or contract entrusting the administration of company debentures concerning OTC convertible debentures including foreign currency denominated convertible debentures.

(1) Notice of the resolution of the board of directors or notice of a determination (1 copy).

Immediately after the decision or determination.

(2) Copy of the contract concerning a change in the trust contract, underwriting contract or contract entrusting administration of debentures with attached proof of the original (1 copy).

Immediately after the change of the contract.
x. Redemption and purchase for retirement of OTC sold valuable securities.

(1) Notice of the resolution of the board of directors or notice of a determination (1 copy).

(2) Notice concerning redemption selected by lot of OTC convertible debentures (1 copy).

(3) Notice concerning calling off redemption selected by lot of OTC convertible debentures (1 copy).

(4) Notice concerning allocation to purchase and write off or bringing down under the debt reduction fund (1 copy).

(5) Notice of determination of a lottery number for redemption selected by lot of OTC convertible debentures (1 copy).

(6) Application for changed registration and written consent (1 copy).

(7) Report of purchase and write off (1 copy).

y. Extraordinary suspension of the transfer of title to stock.

(1) Notice of the resolution of the board of directors (1 copy).

z. JASDA member concluding the basic underwriting agreement for subscription or sale and the issue price or sale price.

aa. Conversion of convertible debentures traded on the OTC market to stock.

(1) Valuable Security Conversion Report (1 copy).

(2) Large Quantity Conversion Report of OTC Convertible Debentures (1 copy).

(3) Samples of the new share certificates (with a list of samples of the securities attached) (1 copy of each different class).

(4) Notice of conversion (1 copy).
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bb. Loss of the benefit of time or the convening of the creditors, etc., regarding convertible debentures.

(1) Copy of the notice concerning loss of the benefit of time and the written reasons therefor (1 copy). Without delay after receipt.

(2) Copy of the notice convening a creditors meeting (1 copy). Without delay after receipt.

(3) Copy of the notice of resolutions of a creditors meeting (1 copy). Without delay after receipt.

cc. Issuance of debentures other than convertible debentures.

(1) Notice of the resolution of the board of directors (with an outline of the issuance attached) (1 copy). Immediately after the decision.

(2) Schedule for issuing debentures (3 copies). Immediately after the decision.


(4) Prospectus (including a Corrected Prospectus) (2 copies). Immediately after its preparation.

(5) Notice concerning the terms, etc. of issue (1 copy). Immediately after their determination.

(6) Copy of the notice stating that the Valuable Securities Statement is effective (1 copy). Immediately after the notice is accepted.

(7) Copy of the trust certificate with attached proof of the original (1 copy). Immediately after conclusion of the contract.

(8) Copy of the contract entrusting administration of the debentures with attached proof of the original (1 copy). Immediately after conclusion of the contract.

(9) Copy of the contract for underwriting and handling of subscriptions with attached proof of the original (1 copy). Immediately after conclusion of the contract.

(10) Sample of the certificate (1 copy). Immediately after its preparation.
dd. Important matters involving rights, benefits or treatment concerning other valuable securities.

(1) **Allocation of rights.**
   (a) Notice of the resolution of the board of directors calling a shareholder meeting (1 copy).
   (b) Notice of the confirmed date of allocation and explanation of content (1 copy).
   (c) Materials relating to the shareholders meeting (2 copies to each one).

(2) **Adjustment of the conversion price of convertible debentures.**
   (a) Notice of the resolution of the board of directors or notice of a determination (1 copy).

(3) **System of the special sale increase of stock insufficient for a unit.**
   (a) Notice of the resolution of the board of directors (1 copy).
   (b) Materials sent to shareholders concerning the special sale increase system (2 copies to each one).

(4) **Other reports sought by JASDA as considered necessary by it for the administration of sales.**
   (a) Reports necessary to JASDA for the administration of sales.

B. **Report of the Occurrence of the Following Facts:**

(1) A loss caused by disaster or in business operations.*
(2) Change in a major shareholder.
(3) Facts which are the cause of the cancellation of the registration of stock on the OTC market by JASDA.193
(4) Filing of an action with a court involving a demand under a property right, trial and judgment on such an action and conclusion of part or all of a suit on such an action without a trial or final judgment.*
(5) Petition to a court for a provisional disposition order (the equivalent of a temporary restraining order or temporary injunction in U.S. law) to enjoin a business operation or other disposition comparable thereto, trial and judgment on such a petition and conclusion of part or all of the proceeding involving such a petition without a trial or final judgment.*
(6) Cancellation of a license, suspension of business operations or other disposition comparable thereto by an administrative agency under law or an order.

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193. All the grounds for cancellation are listed in Fair Prac. Reg. 2, art. 11.
Changes in a parent company* (defined as a company that substantively owns over half the voting rights in another company).  
Petition or notification for bankruptcy, for the opening of composition, reorganization proceedings or rehabilitation, or for execution of an enterprise security right (hereinafter called “petition for bankruptcy, etc.”) by a creditor or other person outside the company.
Dishonor of a bill or check or a disposition by a bills clearing house suspending transactions (hereinafter called “dishonor, etc.”).
Petition for bankruptcy, etc. involving a parent or subsidiary company.
The fact that the risk of nonperformance of a debt has arisen in regard to a right of indemnification against a major debtor, who is either the obligor himself or the obligor under a guaranty, upon the performance of receivables, loans or other claims against this debtor due to dishonor, etc., a petition of bankruptcy, etc. or other comparable facts.*
Suspension of transactions with a person responsible for not less than 10 percent of the company's total sales or total purchases in the prior business year (called a “major party to transactions”).*
Forgiveness of indebtedness by a creditor and acceptance or satisfaction of a debt by a third party.*
Discovery of a natural resource.*

C. Miscellaneous Reports

A difference that has arisen in comparison between the sales, ordinary profit or net profit of the company in either a newly computed estimate or the closing of the books for the current business year and the most recently published prior estimate or, if there has been no published estimate, the published results of the prior business year.
Any assignment of shares of stock made or received on a third party capital increase allocation during the period of the compact.  
Other important facts than those above concerning the conduct, operations or property of the company that would markedly affect the investment judgment of an investor.

Reports under B and C above shall be submitted immediately after the event.

X. PRESERVATION OF DOCUMENTS AND THEIR AVAILABILITY FOR INSPECTION

The following documents shall be preserved by the JASDA, and made available for inspection by the public for the period indicated:  

1. Documents specified by Securities Exchange Law arts. 25, 27-14 and 27-8 and Securities Exchange Law Enf. O. art. 26:
   a. Copies of the Valuable Securities Report (including copies of Corrected Reports and attachments).  5 years
   b. Copies of the Issue Registration (including copies of a Corrected Issue Registration and attachments).  Until the Issue Registration loses validity

194. Financial Statement Regulations art. 8 (3).
195. Fair Prac. Reg. 2, art. 32; Fair Prac. Reg. 2 Det. Rules art. 16(3); see pages 59-60 infra.

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c. Copies of the Valuable Securities Report (including copies of Corrected Issue Registration and attachments). 5 years

d. Copies of the Half Term Report (including copies of Corrected Reports). 3 years

e. Copies of the Extraordinary Report (including copies of Corrected Reports). 1 year

f. Copies of the Report of the Circumstances of Purchasing One's Own Shares (including Corrected Reports). 1 year

g. Disclosure materials concerning a public purchase:
   (1) Copies of the Public Purchase Statement (including copies of a Corrected Statement).
   (2) Copies of the Statement Withdrawing a Public Purchase.
   (3) Copies of the Public Purchase Report (including copies of a Corrected Statement).

h. Copies of the Large Quantity Holdings Report (including copies of a Revised or Corrected Report). 5 years

2. Documents involved in the registration application.
   a. Valuable Securities Report for the Purpose of the Registration Application. 5 years
   b. Half Term Report for the Purpose of the Registration Application. 5 years
   c. Business and financial reports for the most recent three years. 5 years
   d. Outline of the company. 5 years

3. Other documents felt to be needed by JASDA.
   a. Copies of Valuable Securities Statements (including copies of a Corrected Statement and attachments). 5 years
   b. Prospectuses. 5 years
   c. Brief account of the closing of the books (including interim and consolidated closings). 1 year
   d. Written summaries of merging companies. 1 year
   e. Documents concerning the assignment of shares or return of share certificates involved in a capital increase by allocating shares to third parties (including conversion of convertible debentures and debentures attached to the right to receive new shares or exercise of the right to receive new shares). 5 years
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shares) either before or after registration.

f. Documents involving the publications of reporters.

g. Other documents requested by JASDA such as:
   (1) Written summary of the assignment or receipt of assignment of a business.
   (2) Written summary of the assignment or acquisition of a fixed asset in the business.
   (3) Written summary concerning changes in a subsidiary company.
   (4) Annual reports.

XI. SHAREHOLDER FIVE PERCENT RULE

A person holding over 5 percent of the issued and outstanding shares of a company with registered shares being traded on the OTC market is called a "large holder." This person is required to submit to the Minister of Finance within five days after he becomes a large holder a Large Holdings Report in which are recorded the percentage of shares held, the purpose of the holding, the amount of money invested and other matters. A similar report must be filed within five days after a 1 percent increase or decrease in holdings and a change in any matters other than the percentage of holdings noted in the initial or subsequent reports. A copy of these reports must also be submitted promptly to the JASDA.197

Delay and false statements are subject to criminal penalties of imprisonment at hard labor for up to six months and a fine of up to 500,000 yen.198

XII. INSIDER TRADING

Extensive rules and restrictions have been established regulating trading in shares by officers, major shareholders (page 12 above) and other persons including employees having a special relationship with a company whose shares are registered on the OTC market. Certain transactions are prohibited and others must be reported by the person involved. These rules should be carefully reviewed by all who are concerned that they may be subject to these requirements.199

XIII. CONCLUSION

The above is only a summary of the information and preparation required to seek over-the-counter registration for a foreign related Japanese domestic company and the subsequent follow up reports which must be filed. Many very specific and detailed additional requirements must also be met. For example, the Valuable Securities Statement and Valuable Securities Reports to be filed with the Securities

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Bureau of the Ministry of Finance through its regional Finance Bureaus are very similar to the Registration Statements and 10-K's filed with the SEC in the United States and subject to equally detailed rules and practice as to their content. Competent professional assistance should be sought in the course of preparing these documents. Careful preparation and effort is important in attaining successful registration.