Short sales and Japan's moves to promote transparency and fairness in public share offers

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Speedread

In 2010, the volumes of short selling in shares in Tokyo Electric Power Co. (TEPCO), Nippon Sheet Glass Co. and INPEX Corp increased and share prices of those companies dropped just before they announced their respective capital increase plans. These cases have given rise to speculation both within Japan and overseas that the holders of non-public information relating to fundraising activities and expected falls in share price consequential to such fundraising may be misusing such information.

In 2010, the volumes of short selling in shares in Tokyo Electric Power Co. (TEPCO), Nippon Sheet Glass Co. and INPEX Corp., an oil development company (all listed on the Tokyo Stock Exchange), increased and share prices of those companies dropped just before they announced their respective capital increase plans. These cases and other similar cases have given rise to speculation both within Japan and overseas that the holders of non-public information relating to fundraising activities and expected falls in share price consequential to such fundraising may be misusing such information.

It has been customary practice in Japan for security firms underwriting share issues to conduct demand surveys by contacting investors and providing them with non-public information about the issuer companies. It has been suggested that such practice facilitates the use of short sale trades to profit from the non-public information, even though the Japan Securities Dealers Association (JSDA), a self-regulatory body comprised of securities firms in Japan, has provided rules for such surveys including requirements to obtain agreement from participants regarding confidentiality and trading restrictions. On 24 December 2010, the Financial Services Agency of Japan (FSAJ) announced its "Action Plan to Vitalise the Financial and Capital Markets and Financial Industry", in which it demanded JSDA to consider stricter controls on the use of non-public information relating to companies issuing new shares.

Even short sales that are made after the announcement regarding the issue of new shares is made can distort the pricing mechanism for the new shares and may harm investors' confidence in the fairness and transparency of the market. As such, the FSAJ also announced in the abovementioned Action Plan that they will implement new rules similar to the US SEC Regulation M in the first half of 2011 , which will prohibit the acquisition of new shares where the purchaser has, during the period between the date on which the announcement regarding the issue of the new shares is made and the date on which the price of the new shares is fixed, sold shares in the issuing company.

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