

The financial markets in Japan 2010 and outlook for 2011

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Speedread

This article highlights the most significant developments related to the financial markets in Japan in 2010, as well as looking forward to those to come in 2011.

The Hatoyama cabinet resigned *en masse* on 4 June 2010 with the Kan cabinet being formed shortly after on 8 June 2010. The Kan cabinet succeeded the policies of the Hatoyama cabinet and is continuing to make genuine efforts to implement them as follows:

Japan's Financial Services Agency provides detailed rules on centralised clearance of OTC derivatives, consolidated-basis supervision of securities companies and other rules and published the results of public comment on 21 December 2010. These rules will come into effect on 1 April 2011.

On 10 November 2010, Tokyo AIM, Inc., a subsidiary of Tokyo Stock Exchange Group, Inc. announced that it will establish the "TOKYO PRO-BOND Market" (a bond market for professional investors). The new market will enable issuers to benefit from a speed and flexibility of issuance equivalent to using Euro MTN programmes, by means of simplified disclosure documents and procedures.

In order to deal with high levels of personal debt in Japan, the Amended Money Lending Business Act came into force in stages over a three and a half year period, and was completely in force by 18 June 2010. This amended Act provides for a reduction of the maximum interest rate and introduction of total quantity regulations to prevent excess borrowing and excess lending.

The "Cabinet Office Ordinance on Partial Amendment of the Cabinet Office Ordinance on Disclosure of Corporate Information, etc. (2010 Cabinet Office Ordinance No.12)" which sets out rules regarding full disclosure of corporate governance of listed companies, was proclaimed and came into effect on 31 March 2010.

Expected major reforms in financial sector in 2011

Six months have passed since the Kan cabinet came into office on 8 June 2010. Since then, its major advance in the reform of the financial sector was its adoption of the "New Growth Strategy" at a Cabinet meeting held on 18 June 2010.

As the next step for carrying out the strategy, the Financial Services Agency of Japan (FSAJ) published the "Action Plan for the New Growth Strategy" (the Action Plan) on 24 December 2010, which has the predominant aims of:

Enabling appropriate finances for corporations in accordance with their scale.

Enabling Japan's market to be a financial centre for Asia.

Enactment and amendment of financial regulations to enable investors to invest their assets efficiently and effectively.

The key financial measures which the FSA proposed to be taken in its Action Plan are as follows:

Permitting banks and insurance companies to engage in finance lease business (which only subsidiaries thereof were permitted to engage in under the Banking Act and Insurance Business Act).

Establishing the "TOKYO PRO-BOND Market" during 2011.

Simplifying the disclosure process and the contents of quarterly reports.

Permitting foreign companies to make disclosure via offering documents written in English when they issue bonds by public offering.

Amending the Financial Instruments and Exchange Act and some related regulations to make the process of rights issues smoother.

Introducing tax initiatives to permit companies to issue Islamic bonds within Japan.

Making the Japanese Bond Income Tax Exemption Scheme which treats interest and profit from redemption of corporate bonds in book-entry form received by non-residents exempt from tax, a permanent tax system.

Commercial and Corporate sector

Legislative initiatives

Amendments to the Copyright Act facilitate the circulation of digital contents and access to and use of copyright works within Japan by permitting exploitation of copyright materials on the Internet, prohibiting the downloading of illegal audio or visual recordings of copyright materials through the Internet for private use if the person downloading the material knows that the material was created without a license and providing physically disabled persons with the opportunity to access copyright materials.

Amendments to the Cabinet Office Ordinance on Disclosure of Corporate Information, etc. came into effect on March 2010 and require that security reports of listed companies contain, amongst other items:

An outline of the governance system adopted by the relevant company and an explanation of why such system was adopted.

Disclosure regarding the names of and amounts of remuneration paid to directors and statutory auditors where such person's remuneration for the relevant fiscal year is JPY100 million or more.

The total amount of shares for the current and previous fiscal year which the company holds solely for the purpose of realising direct investment gains.

Case law

In 2010, the courts made the following important rulings:

The imposition of:

inheritance tax on the lump sum paid under a life insurance policy;

income tax on the annual payments made to the relevant beneficiary under the policy constituted double taxation and therefore in breach of Japanese tax laws.

In a case involving the purchase of shares by a company in its subsidiary (as part of a restructuring) for a price much higher than their alleged true value, the directors of the purchaser were sued by the company's shareholders for damages in an amount equal to the difference between the price paid and the true value of the shares. The Supreme Court held that the director's were not liable and applied the business judgment rule under which it acknowledged a broad discretion of directors in the restructuring of group companies.

Expected major reforms in Corporate sector in 2011

It was expected at the beginning of 2010 that the proposed enactment of the Public Company Act (an Act regulating of Public Company) would be the subject of much discussion and consideration by the ruling Democratic Party of Japan, but this has, in fact, not been the case. Instead, insofar as corporate law is concerned, the DPJ's focus has been on amending the regulations affecting the parent-subsidiary and this has resulted in the Justice Ministry's Legislative Council Corporate Law Subcommittee which has as its agenda: (1) protection of parent company's shareholders, (2) protection of subsidiary company's shareholders and creditors and (3) regulation of the procedures applicable to the formation of business combinations. However, it is not certain that these amendments will come into effect.

The agendas focus on the following:

Protection of parent company's shareholders.

Allowing shareholders to bring derivative actions against the company's subsidiaries.

Improving shareholder access to information generated by subsidiary companies.

Providing for shareholders to be involved in subsidiaries' decision-making processes.

Protection of subsidiary company's shareholders and creditors

Imposing liability on a parent company where it inappropriately exercises voting rights at meetings of a subsidiary's shareholders and causes damage to the subsidiary company's business.

Providing subsidiary company's shareholders an appraisal right in the event that a new controlling shareholder emerges.

Imposing liability on a company for the salaries payable to employees of a subsidiary where the parent company acts in its own interest to the detriment of the subsidiary company.

Regulation of the procedures applicable to the Formation of Business Combinations

Amendments in relation to the regulation of cash out and incorporation of new institution to execute cash out.

Revision of appraisal rights.

Revision of right of minority shareholders to injunctive relief.

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