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Evolving legislation and enforcement tactics continue to transform the landscape, as highlighted by recent amendments to China's Anti-monopoly Law and an uptick in private antitrust cases in Japan; meanwhile, the Korea Fair Trade Commission has updated its Guidelines on Merger Filing to expedite the review process.

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Japan: JFTC establishes jurisdiction over M&A transactions under the Anti-monopoly Act

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Summary

IN SUMMARY

This article provides an overview of the merger control landscape in Japan, including information on thresholds for notification, safe harbours and foreignto- foreign transactions, among other topics.

DISCUSSION POINTS

- Mergers, business transfers, demergers and M&A transactions all subject to prior notification
- Domestic sales a decisive factor in M&A notification thresholds
- M&A transactions subject to standard 30-day waiting period

REFERENCED IN THIS ARTICLE

- Anti-monopoly Act
- Japan Fair Trade Commission
- Merger Rules
- Merger Guidelines

INTRODUCTION

Merger control was introduced in Japan by Act No. 54 of 1947, as amended – otherwise known as the Anti-monopoly Act (AMA)[1] – at the same time as Japan's first competition rules. The Japan Fair Trade Commission (JFTC)[2] has primary jurisdiction over the enforcement of merger control under the AMA. The AMA provides two types of regulations for business combination:

- a formalistic regulation that requires a prior notification for transactions that satisfy the relevant thresholds; and
- a substantial regulation that prohibits a business combination that will result in substantial restraint of trade in a particular field of trade (relevant market).

PRIOR NOTIFICATION REQUIREMENT

Transactions To Be Notified

Mergers, business transfers, corporate splits (demergers) and stock acquisitions (mergers and acquisitions (M&A) transactions) are all subject to prior notification under the AMA. M&A transactions whose schemes involve more than one of these transactions (eg, where an acquirer merges with a target after acquiring shares in the target) are separately analysed at each step of the transaction, so separate filings may, in principle, need to be made for the various steps. Joint ventures are also analysed in the same way.

If the M&A transactions satisfy certain thresholds, they are subject to a prior notification obligation. Generally, M&A transactions within the same combined business group are exempted from the prior notification requirement.

In 2013, the JFTC clarified its practice regarding mergers. Under the new practice, in case of an absorption-type merger where Company A merges into Company B and shares of Company B will be issued to the shareholders of Company A, the JFTC requires a notification of a merger between Company A and Company B, as well as a notification of stock acquisition by the shareholders of Company A.

THRESHOLDS FOR NOTIFICATION

Stock Acquisitions

A stock acquisition will require a prior notification if the stockholding ratio after the transaction rises above 20 per cent or 50 per cent and the following turnover thresholds are satisfied.

Role	Threshold
Acquiring corporation	The aggregate domestic sales of all corporations within the same combined business group as the acquiring corporation exceed ¥20 billion.
Target corporation	The aggregate domestic sales of the target corporation and its subsidiaries exceed ¥5 billion.

Business Transfer (including Corporate Splits)

The filing thresholds for business transfers (including asset transfers and corporate splits) are as follows. Note that if a business transfer is implemented by a corporate split under the Corporate Act of Japan, different filing thresholds apply.

Transfer Of Whole Business

Role	Threshold
Acquiring corporation	The aggregate domestic sales of all corporations within the same combined business group as the acquiring corporation exceed ¥20 billion.
Transferring corporation	The domestic sales exceed ¥3 billion.

Transfer Of A Substantial Part Of The Business, Or The Whole Or A Substantial Part Of The Fixed Assets Used For The Business

Role	Threshold
Acquiring corporation	The aggregate domestic sales of all corporations within the same combined business group as the acquiring corporation exceed ¥20 billion.
Transferring corporation	The domestic sales attributable to the transferring business or assets exceed ¥3 billion.

Mergers

The filing thresholds for mergers are as follows:

- the aggregate domestic sales of all corporations within the same combined business group as one of the merging companies must exceed ¥20 billion; and
- the aggregate domestic sales of all corporations within the same combined business group of one of the other merging companies must exceed ¥5 billion.

DOMESTIC SALES

As can be seen from the above, domestic sales are a decisive factor in the threshold. Domestic sales are defined as the total amount of prices of goods or services supplied in Japan during the latest fiscal year (article 10,
paragraph 2 of the AMA). According to the Rules on Applications for Approval, Reporting, Notification, etc. Pursuant to articles 9 to 16 of the Act on Prohibition of Private Monopolisation and Maintenance of Fair Trade, published by the JFTC (the Merger Rules), domestic sales of Company X include the sales amount accrued through direct importing to Japan and, more precisely, will be the total amount of the following three categories of sales (article 2, paragraph 1 of the Merger Rules):

- the sales amount of goods with respect to which domestic consumers (individuals excluding those who are transacting for business) are the purchasers;
- the sales amount of goods to be supplied in Japan with respect to which corporations or other business entities or individuals who are transacting for business (business entities) are the purchasers (provided, however, that the sales amount of goods that Company X knows, at the time of entering into the relevant contract, will be further shipped outside Japan without any changes in their nature or physical appearance, should be excluded); and
- the sales amount of goods to be supplied outside Japan with respect to which business entities are the purchasers and which Company X knows, at the time of entering into the relevant contract, will be further shipped to Japan without any changes in their nature or physical appearance.

The same threshold will be used regardless of the jurisdiction in which the acquiring corporation or the target corporation was established. It should be noted that, if Company X is a company obliged to submit financial statements (article 5, paragraph 1, item 1 of the Rules regarding the Terms, Forms and Preparation Methods of Financial Statements, etc), it may substitute the value as determined pursuant to the Merger Rules as their domestic sales (article 2, paragraph 2 of the Merger Rules).

It should also be noted that the Merger Rules have a provision to allow flexibility where the strict calculation of domestic sales in accordance with the Merger Rules is not possible, in which case it is permitted to use a different method to calculate the amount of domestic sales, provided that it is in line with the purpose of the above method and in accordance with generally accepted accounting principles (article 2, paragraph 3 of the Merger Rules).

COMBINED BUSINESS GROUP

The combined business group comprises the ultimate parent company and all of its subsidiaries. A corporation will be considered to be a subsidiary not only when more than 50 per cent of the voting rights of the corporation are held by another corporation, but also if

its management is 'controlled' by the other corporation (article 10, paragraph 6 of the AMA). The Merger Rules specify a detailed threshold for 'control' that might be found to be met even if the ratio of beneficially owned voting rights is 50 per cent or below. The concept of control as used to decide the scope of subsidiaries is in line with the concept of control as used to define group companies under the Ordinance for the Enforcement of Companies Act, and therefore it is not a totally new concept. However, it is a concept slightly different from the concept of control under the regulations for financial statements. Moreover, according to a reply by the JFTC to public comments announced on 23 October 2009, the scope of the 'combined business companies' should be decided immediately before the closing of the transaction. Therefore, it may not be possible to use the list of group companies as written in the relevant financial statements, and companies should at least check whether the list of group companies is exactly the same as requested by the Merger Rules, which could take considerable time depending on the complexity of the corporate structure of the company in question. A partnership can be a subsidiary under the AMA but cannot be a parent company. Voting rights held by a partnership are regarded as being held by the parent company of the partnership. Also, a corporation that owns the majority of rights to execute business operations of a partnership (normally, a general partner) is a parent company of the partnership regardless of its participation ratio. Therefore, if more than 50 per cent of voting rights in Company X are held by Partnership Y, General Partner Z of Partnership Y is regarded as holding those voting rights and thus a parent company of Company X (and Company X and Partnership Y are subsidiaries of General Partner Z).

WAITING PERIOD

M&A transactions are subject to a standard 30-day waiting period (or, if this period is shortened, within the shortened period). The JFTC may formally request additional information during this period (second request).

If the JFTC considers that the contemplated M&A transaction has an anticompetitive effect and therefore intends to order certain necessary measures be taken, it will notify the party within the 30-day waiting period or, if the JFTC issues a second request, within the longer period of either 120 days from the date of receipt of the initial notification or 90 days from the date of the receipt of all responses to the second request.

If the JFTC considers that the contemplated M&A transaction does not have an anticompetitive effect, it will provide a clearance letter to the party within the above-mentioned period. In addition to the statutory waiting period, it takes some time for the parties to prepare a draft notification by collecting, for example, market data, and for the JFTC to check the draft and to formally accept the notification. If the M&A transaction has any anticompetitive effect, the period necessary to consult with the JFTC prior to the notification also needs to be taken into consideration. In practice, it normally takes two to four weeks for such preparation even where the M&A transaction does not have any anticompetitive effect. If the M&A transaction has any anticompetitive effect, the preparation takes longer (approximately two to six months).

SUBSTANTIVE TEST

The Nature Of The Substantive Test For The Assessment Of Mergers

It is important to note that the JFTC can theoretically review any M&A transaction under the substantive test regardless of whether or not the thresholds described above are met. In fact, the JFTC recommends in the Guidelines Concerning Procedures of Review of Business

Combination that certain M&A transactions that do not meet the filing thresholds but of which the acquisition value exceeds ¥40 billion and has a local effect should be voluntarily notified before the M&A transactions complete. The substantive test for clearance is whether the proposed M&A transaction may result in a 'substantial restraint of competition in a particular field of trade'. The Guidelines to Application of the Anti-monopoly Act Concerning Review of Business Combination (the Merger Guidelines) provide guidance as to the substantive test.

Regarding market definition, the Merger Guidelines in principle adopt the small but significant and non-transitory increase in price test for the purposes of analysing demand and supply substitution. However, if quality competition mainly occurs instead of price competition in, for instance, the market for internet-related service, the small but significant and non-transitory decrease in quality test or small but significant and non-transitory increase in cost test is adopted.

Importantly, the Merger Guidelines clarify that the geographical market may be wider than the geographical boundaries of the territory of Japan, depending upon the international nature of the relevant business. The JFTC has actually defined the 'relevant market' as the global market in cases such as the market for magnetic heads (acquisition of fixed assets for magnetic head manufacturing from Alpus Electric Co Ltd by TDK Corporation), the markets relevant for semi-conductors such as SRAM, MCUs, LCD drivers, transistors and thyristors (merger of NEC Electronics Corporation and Renesas Technology Corporation) and HDD (consolidation plan of manufacturing and sales companies of hard disk drives).

In addition, the Merger Guidelines explain the factors that will be taken into account when assessing whether a certain M&A transaction substantially restrains competition in a relevant market. The substantive test is analysed in each case for horizontal, vertical and conglomerate M&A transactions.

Perhaps the most interesting feature of the Merger Guidelines is the use of safe harbours for each of the three categories of M&A transactions identified above (specific harbours apply to each category) as part of the substantive test analysis. These are cases where the JFTC normally considers that there is no possibility that there may be a substantial restraint of competition or that such a possibility is small and, accordingly, it is not necessary to conduct a detailed examination of the M&A transaction. Each case is, however, reviewed on its own merits and the application of the harbours needs to be analysed carefully within the specific context of each transaction. In particular, the JFTC tends to define narrower markets for the safe harbour assessment because, as mentioned above, once the transaction meets the safe harbour thresholds, the JFTC loses grounds on further substantive review. The Merger Guidelines also clarify that, in cases where the parties have significant potential competitive power that is not reflected by market shares by owning competitively material data or intellectual property rights, the JFTC will still conduct a substantive review for M&A transactions that meet the safe harbour thresholds.

SAFE HARBOURS

Safe Harbours For Horizontal M&A Transactions

In the case of horizontal M&A transactions, if any of the following three conditions is satisfied (and there are no other competitive restrictions), the JFTC is likely to consider that the M&A transaction does not substantially restrain competition in a relevant market:

- the Herfindahl-Hirschman Index (HHI) after the M&A transaction is not more than 1,500;
- the HHI after the M&A transaction exceeds 1,500 but is not more than 2,500 and the HHI does not increase (the delta) by more than 250; or
- the HHI after the M&A transaction exceeds 2,500 and the delta is not more than 150.

If none of the above safe harbours is met, the JFTC will proceed with a (separate) analysis of the non-coordinated (unilateral) and coordinated effects of the horizontal M&A transaction. However, the Merger Guidelines clarify that, based on the JFTC's past experience, if the HHI after the completion of the M&A transaction is not more than 2,500 and the combined market share does not exceed 35 per cent, it is generally considered that there is a low possibility that the M&A transaction will substantially restrain competition.

SAFE HARBOURS FOR VERTICAL AND CONGLOMERATE M&A TRANSACTIONS

The Merger Guidelines identify two safe harbours for vertical and conglomerate M&A transactions. The JFTC is likely to consider that the M&A transaction does not substantially restrain competition in a relevant market if any of the following conditions is met (and there are no other competitive restrictions):

- the merging parties' market share in each of relevant markets (eg, in both the upstream and downstream markets for vertical M&A transaction) after the M&A transaction is not more than 10 per cent; or
- the merging parties' market share in each of relevant markets after the M&A transaction is not more than 25 per cent and the HHI after the M&A transaction is not more than 2,500.

If neither of the above safe harbours is met, the JFTC will proceed with a (separate) analysis of the non-coordinated (unilateral) and coordinated effects of a vertical or conglomerate M&A transaction. However, the Merger Guidelines clarify that if, in each of relevant markets, the HHI after the M&A transaction is not more than 2,500 and the merging parties' market share after the M&A transaction is not more than 35 per cent, it is generally considered that the possibility of the M&A transaction resulting in substantial restraint of competition is low.

M&A TRANSACTIONS THAT DO NOT SATISFY THE SAFE HARBOUR

Analysis Of Unilateral And Coordinated Effects Of Horizontal M&A Transactions

The Merger Guidelines specify the following as the determining factors in examining the unilateral effects of a horizontal M&A transaction:

- the position of the company group and the competitive situation – such as market shares and market share ranks, competition among the parties in the past, market share differences between the competitors and the parties, competitors' excess capacity, degree of differentiation of products, status of the parties' research and development regarding competitive products and market characteristic such as network effect and economies of scale;
- import – degree of institutional barriers to import products, degree of import-related transportation cost and existence of problems in distribution, degree of

substitutability between the imported product and the parties' product, and whether it is feasible to supply from overseas;

- entry – degree of institutional barriers to enter the market, degree of practical barriers to enter the market, degree of substitutability between entrants' product and the parties' products, and potential entry pressure;
- competitive pressure from adjacent markets – what are the competing goods, and the situation of the geographically adjacent market;
- competitive pressure from users – competition among users and ease in changing suppliers;
- overall business capabilities; and
- efficiency – whether the M&A transaction improves efficiency, whether the improvements in efficiency are achievable and whether the improvements in efficiency contribute to the interests of users.

The Merger Guidelines also specify the following as the determining factors in examining whether a horizontal M&A transaction may substantially restrain competition in a relevant market through coordinated conduct:

- the position of the company group and the competitive situation – such as the number of competitors, competition among the parties in the past and excess capacity of competitors;
- actual condition of trade – ease of obtaining information regarding price and quantity of the competitors' trade, trends in demand and technological innovation, and past competitive situation;
- competitive pressure from import, entry and adjacent markets and so on; and
- efficiency – whether the M&A transaction improves efficiency and whether the improvements in efficiency are achievable or contribute to the interests of users.

FAILING-FIRM DEFENCE

The failing-firm defence is available under the Merger Guidelines as a defence to a horizontal M&A transaction. The Merger Guidelines stipulate that the possibility that the effect of a horizontal business combination may substantially restrain competition is usually small if:

> [a] party to the combination has recorded continuous and significant ordinary losses or has excess debt or is unable to obtain finance for working capital and it is obvious that the party would be highly likely to go bankrupt and exit the market in the near future without the business combination. Moreover, it is difficult to find any business operator that can rescue the party with a combination that would have less impact on competition than the business operator that is the other party to the combination.

Based on this failing-firm defence, the JFTC cleared the proposed acquisition of shares of Showa Aluminium KK by Toyo Aluminium KK (see the press release of the JFTC on 28 December 2010).

PRIOR CONSULTATION PROCEDURE

When a party plans to implement an M&A transaction that may raise substantive issues, the party may first consider consulting with the JFTC at the pre-notification stage. Although the Policies Concerning Procedures of Review of Business Combination published by the JFTC in 2001 state that the consultation system at the pre-notification stage is mainly to assist parties with filling in the notification form, since the notification form includes some items that are crucial for substantive issues such as market definition and market share, the parties may discuss substantive issues with the JFTC in connection with such items. In practice, during the pre-notification stage, the JFTC comments on the data provided in the notification form by the parties, starts to review the substantive issues and asks substantive questions to the parties. The parties can also proactively communicate with the JFTC, for example, by requesting the JFTC to explain certain issues in order to understand concerns at an early stage and by submitting written opinions as to how they plan to address such concerns.

FOREIGN-TO-FOREIGN TRANSACTIONS

After the amendment to the AMA, effective as of 31 January 2010, the thresholds capture domestic sales by a foreign company that does not have a subsidiary in Japan and any foreign-to-foreign transactions should be notified if they satisfy the thresholds.

It appears that the JFTC will not hesitate to investigate a foreign-to-foreign transaction if it will result in substantial restraint of competition. As mentioned above, the JFTC may open an investigation when it finds substantive issues regardless of whether the transaction satisfies the notification thresholds or not. For example, in 2008, the JFTC opened investigations in relation to the acquisition by BHP Billiton of shares issued by Rio Tinto, which was a purely foreign-to-foreign transaction, and actively investigated the transaction.

In order to facilitate the investigation of international transactions, the JFTC has entered into an anti-monopoly cooperation agreement with each of Canada, the European Community and the United States. In addition, the JFTC has entered into economic partnership agreements with various countries such as Australia, Chile, India, Indonesia, Malaysia, Mexico, Mongolia, Peru, the Philippines, Singapore, Switzerland, Thailand, the United Kingdom and Vietnam.

Endnotes

[1] The AMA is accessible via the JFTC's website.

[2] More information the JFTC can be found on its website.

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