

A Brief Guide to Japanese Proxy Solicitations

Corporate Department

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Many aspects of conducting a proxy solicitation involving a Japanese company are similar to those of the United States. However, activist shareholders should be aware that there are important differences. The following is a brief outline of the significant aspects of conducting a proxy solicitation involving a Japanese company.¹

The Proposal

The first consideration facing activist shareholders who wish to conduct a proxy contest involving a Japanese company (the “Subject Company”) is whether they have the right to put forth a proposal at the Subject Company’s shareholder meeting, either the annual general meeting or an extraordinary general meeting (the “Shareholders Meeting”). A shareholder who is registered in the Subject Company’s shareholder registry at the time of submission must have either:

- (i) held at least 1% of all the Subject Company’s voting rights for six months or more; or
- (ii) held voting rights equal to or greater than 300 shares for six months or more,

in order to have the right to put a resolution onto the agenda for a Shareholders Meeting.

Shareholders are required to submit their proposal eight weeks prior to the Shareholders Meeting. Generally, however, the date of a Shareholders Meeting is not known until the Subject Company delivers a convocation notice to shareholders. The typical practice is for the Subject Company to send shareholders a convocation notice two to three weeks prior to the Shareholders Meeting (by law, the notice cannot be sent later than two weeks prior to the meeting). This makes it very difficult for an activist shareholder to wait until after the meeting date is known to submit a proposal. A shareholder is, however, permitted to propose an agenda item before knowing when a Shareholders Meeting will take place.

Proposals Involving the Election of Directors

If the proposal involves the nomination of directors, the Subject Company, at its sole discretion, may incorporate it into its Shareholders Meeting agenda in one of two ways:

- (i) have a combined agenda in which shareholders select the required number of directors from all candidates (including the activist’s nominees); or

¹ This memo represents a summary of information Olshan Grundman Frome Rosenzweig & Wolosky LLP has received from various Japanese counsel and from our own experience working with Japanese counsel in Japanese activist matters. Olshan Grundman Frome Rosenzweig & Wolosky LLP does not have a Japanese legal practice nor does it employ lawyers who are licensed to practice in Japan..

- (ii) more commonly, have two separate agendas in which shareholders may either vote for the Subject Company's slate of directors or for the activist's slate.

If an activist shareholder does not want a particular group of directors to be re-elected, it is important that the activist's proxy form specifically name the directors that will not be voted for. Note that if the Subject Company's Articles of Incorporation does not cap the number of directors who are able to serve, then all director candidates who receive greater than 50% of the votes cast will be elected. If the Articles of Incorporation does set a limit on the number of directors who may be elected, shareholders should be aware that only those nominees who receive the highest number of votes will be elected, assuming each receives a majority of the votes cast.

Persuasion versus Proxy Solicitation

Once an activist shareholder has submitted a proposal, the shareholder must decide whether to conduct a "Proxy Solicitation" or "Persuasion." A Proxy Solicitation is a soliciting activity, the purpose of which is to obtain a proxy from another shareholder in connection with one or more resolutions. A Persuasion is limited to activities that are aimed at persuading shareholders to cast their own votes in support of the matters contained in the activist's proposal without requesting a proxy. For example, encouraging shareholders to send voting slips to the Subject Company in favor of the activist's slate of directors would be deemed a Persuasion, not a Proxy Solicitation. A shareholder may conduct any and all activities that may be considered Persuasion without triggering the Proxy Solicitation regulations.

An activist shareholder must be careful when conducting a Persuasion because the activist runs the risk that a regulator may decide that the Persuasion activities were also aimed to achieve (and formed part of) a Proxy Solicitation, if the activist follows the Persuasion with a formal Proxy Solicitation.

Conducting a formal Proxy Solicitation has some advantages over a Persuasion, including increased media attention and increased pressure on the Subject Company's management.

Pre-Solicitations

It may be difficult or impossible for an activist shareholder to commence a Proxy Solicitation before receiving a convocation notice from the Subject Company or before the Subject Company announces the Shareholders Meeting agenda, because management tends to send convocations two or three weeks before a Shareholders Meeting. As a result, activist investors should consider conducting a "Pre-Solicitation" prior to the Proxy Solicitation.²

Shareholders wishing to conduct a Pre-Solicitation campaign should consider the following activities:

- sending letters to shareholders of the Subject Company;

² As an added precaution, shareholders interested in conducting a Pre-Solicitation campaign may "unofficially" contact government regulators to see whether such designated actions may fall within the Proxy Solicitation regime.

- telephoning shareholders of the Subject Company;
- publishing an open letter to management;
- conducting media interviews; and
- making the proposal available on a website.

All documents and communications used in the Pre-Solicitation campaign should be carefully reviewed and clearly drafted so as not to contain any false or misleading statements. Additionally, activists should ensure that each of their Pre-Solicitation written communications with shareholders clearly state that:

- the document is not itself a proxy request;
- the activist shareholder has not decided whether it will conduct a Proxy Solicitation; and
- because these activities are not Proxy Solicitations, the activist shareholder will return any documents sent to it by shareholders that purport to be proxies.

With respect to oral communications with shareholders (including indirect communications such as media interviews), activists should ensure that such communications do not contain any inference that the activist is conducting a Proxy Solicitation.³

Proxy Solicitation Requirements

Once an activist shareholder begins soliciting proxies the Proxy Solicitation Regulations under the Enforcement Rules of the Financial Instruments and Exchange Law (Law No. 25 of 1948 as amended) (the “Regulations”) apply. In brief, the Regulations require:

- that proxy forms and statutory information documents (the “Proxy Documents”) must be provided to solicited shareholders;
- that all Proxy Documents be filed with the Kanto Local Finance Bureau (the “Regulator”) before the being distributed to shareholders; and
- that the Proxy Solicitation (including any Proxy Documents) must not contain any false or misleading statements.

All methods of solicitation (including website-based solicitations and emails) are subject to the Regulations.

Additionally, an activist shareholder should be aware that, as a practical matter, the Regulator will require:

- (i) the submission to the Regulator of all other documents to be sent to shareholders (e.g., cover letters) in addition to the Proxy Documents; and

³ Activists who are considering providing oral communications, such as telephone campaigns, should do so from a prepared script and, to counter any accusations that the oral communications were tantamount to Proxy Solicitation, record such communications to the extent possible.

- (ii) prior approval by the Regulator for all documents filed with the Regulator in connection with the Proxy Solicitation (including the Proxy Documents) that are to be sent to shareholders.

Voting against the Subject Company's nominees in an election contest

In addition to soliciting votes for their own proposal, shareholders may also oppose the approval of the Subject Company's proposal. This is critical in cases where the Subject Company has a cap on the number of directors who may serve on the board. In these cases, the activist shareholder should make sure to identify which of the Subject Company's nominees they will oppose, to help reduce the possibility of the Subject Company's nominees being elected. As a practical matter, this may prove difficult because the Subject Company may not make the final list of nominees public until a few weeks before the Shareholders Meeting. As an alternative, activists may want to consider opposing the Subject Company's entire slate of nominees. This may work in the activist's favor by preventing the Subject Company's nominees from being properly elected. For example, at a shareholders meeting earlier this year, seven of the incumbent directors of Aderans Holdings up for election did not receive a majority of the votes cast, which prevented the incumbent directors from being re-elected to the Board under Japanese law.

Who may help conduct Proxy Solicitation?

Activist shareholders may enlist third parties to help with their Proxy Solicitation without receiving permission from Regulators. However, if the activist plans to engage a licensed securities firm, the firm may first have to obtain regulatory approval before providing their services, because Japanese law requires that securities firms receive approval before conducting non-securities-business, unless that non-securities-business is ancillary to its core securities business. If the shareholder retains another party to help conduct the Proxy Solicitation, solicitation materials should be jointly filed with the Regulator by both parties.

Who can attend the Shareholders Meeting?

Japanese companies have the ability to limit who may receive a shareholder's proxy. For example, the Subject Company may provide in its Articles of Incorporation that only a shareholder may serve as another shareholder's proxy. Activists should carefully review a Subject Company's Articles of Incorporation to determine if any special provisions exist. Note that if the activist shareholder is a corporation or another entity, an authorized employee or officer would be allowed to attend the Shareholders Meeting on behalf of that corporation. There is the possibility that the Subject Company may successfully prohibit an external lawyer retained by an activist shareholder from attending the Shareholders Meeting on behalf of that shareholder. However, if the activist shareholder is a foreign shareholder, its "standing agent" may attend the Shareholders Meeting. Therefore, if a foreign shareholder would like its external lawyer to attend the Shareholders Meeting as its agent, such shareholder should consider registering the lawyer with the Subject Company as its standing agent.

Proxy Form

Only those shareholders who hold voting rights at the Shareholders Meeting, i.e., shareholders whose names are listed on the Subject Company's shareholder register as of the record date, may execute proxy forms. Activists should ensure that voting shareholders affix their registered seal on their proxy, otherwise the Subject Company may treat such proxies as

invalid. If shareholders forget or otherwise fail to use their registered seals to execute proxies, the activist shareholder would have to demonstrate, through the courts, that such failure was merely an oversight and that such proxies were in fact executed. Note that a foreign shareholder's registered seal is held by its standing agents.

Under the Regulations, each proxy form must have two columns for each relevant resolution: one column for voting in favor of that resolution and another column for voting against that resolution. If a shareholder returns a proxy without a definitive statement as to how to vote, then the activist may treat that proxy as a blank proxy that provides full voting discretion; activists should ensure that their form of proxy contains a clear statement to that effect.

If an activist receives an executed proxy that instructs the activist to vote contrary to its proposal, the activist will not be obliged to vote those proxies at the Shareholders Meeting if the activist clearly informed each solicited shareholder that it would not accept any proxies that are contrary to its proposal. To guard against potential complications, the activist should provide very specific conditions in its Proxy Documents as to the conditions under which such proxies will not be accepted.

Presentations at the Shareholders Meeting

In situations where a Proxy Solicitation has a high likelihood of success, the activist shareholder may argue that it is reasonable to allow it a chance to explain its proposal on behalf of all shareholders who have provided it with proxies, prior to the voting at the Shareholders Meeting. Note that under Japanese law this is not an inherent right and, accordingly, the Subject Company would be within its rights to lawfully reject the request to make such a speech/presentation.

OTHER ISSUES

Access to the Subject Company's Shareholder Registry

Under Japanese law, any shareholder may request to copy the Subject Company's shareholder register, as long as the request is not:

- (i) for a purpose other than that of exercising that shareholder's rights;
- (ii) for the purpose of preventing the Subject Company from conducting its business or for damaging shareholders' common interests;
- (iii) from a business competitor of the Subject Company;
- (iv) for the purpose of providing shareholders' information contained in the register to a third party; or
- (v) from a shareholder that has previously provided shareholders' information contained in the register to a third party in the last two years.

Activists should note that if the request is for Pre-solicitation campaign activities, a Subject Company could reject the request on the basis that the request is not for the purpose of exercising its shareholder rights.

Voting Slips

As long as there are 1,000 or more shareholders of the Subject Company, the Subject Company is required to send a voting slip to each shareholder, so that each shareholder may vote for or against each agenda item without attending the Shareholders Meeting. A voting slip form is attached to each convocation notice.

A potential problem could arise if a shareholder has sent a completed proxy to the activist but has also sent a voting slip to the Subject Company that is inconsistent with the completed proxy. If the date stated in the voting slip is clearly later than the date stated on the proxy, the Subject Company may be able to argue that the proxy was withdrawn by the voting slip. An activist should consider meeting with the Subject Company prior to the Shareholders Meeting to discuss a procedure for dealing with such situations. Without an agreement, either the Subject Company or the activist could seek a court decision on how to deal with incompatible proxy forms/voting slips.

The Subject Company is entitled under Japanese law to insert a requirement into its internal rules that a person conducting Proxy Solicitation must also collect voting slips from each shareholder who provides a proxy. If the Subject Company has such a rule in place, the activist should refrain from commencing a Proxy Solicitation until the form of voting slip has been dispatched.

Court Appointed Observer

A shareholder who has held 1% or more of all voting rights for six months or more is entitled to apply to the court for the appointment of an observer (*kensayaku*) to attend a Shareholders Meeting. The activist may seek reimbursement from the Subject Company for some expenses for making an application to the court to appoint the observer. If an observer is appointed, the activist should meet with the Subject Company and the observer to establish ground rules for the Shareholders Meeting.

Foreign Shareholders

If an activist is a foreign shareholder, the activist has the right to have its representative, employee, or a standing agent attend the Shareholders Meeting to exercise voting rights on behalf of shareholders who have granted the activist their proxy. If the representative or employee of a foreign shareholder cannot attend the Shareholders Meeting for any reason, a standing agent would need to attend the Shareholders Meeting in order to exercise voting rights on behalf of those proxies.

If the Subject Company has a substantial number of foreign shareholders, then the activist should arrange for the convocation notice and voting slip (and other Proxy Documents) to be translated into those shareholders' native language because the short period between the delivery of the convocation notice and Shareholders Meeting may not allow shareholders sufficient time to translate the documents themselves. As with all Proxy Documents, such translated documents (including the voting slip and proxy form) should be filed with the

Regulator. Additionally, the translated documents should indicate that the translations were made by the activist shareholder, not the Subject Company.

If the activist chooses to focus its campaign activities on foreign shareholders (on the basis that foreigners may be more amenable to the activist's proposals than would domestic shareholders), then the activist should be sure to explain:

- (i) that a proxy vote is possible under Japanese law;
- (ii) that the shareholder may have limited time to decide to vote, given the Japanese system; and
- (iii) the likely time that a vote and decision will need to be made based on the likely date of the Shareholders Meeting.

Market Manipulation

As a Proxy Solicitation may have an impact on the price of the Subject Company's traded securities, the activist should take care to ensure that any such activities may not be deemed by any regulatory body as market manipulation under Japanese Financial Instruments and Exchange Law. To that end, the activist and its affiliates should consider halting all trading in the Subject Company's shares or other instruments during any such activities and be particularly careful not to make any misstatements in any materials or in any oral communications.

Significant Shareholding Report

Much like 5% shareholders of United States public companies, shareholders who own more than 5% of a Japanese public company's outstanding shares have reporting and disclosure obligations. Depending on their intentions, activist shareholders may wish to or be required to make their actions public in their significant shareholder report.

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