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Japan
Technology M&A

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This country-specific Q&A provides an overview of technology m&a laws and regulations applicable in Japan.

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Japan: Technology M&A

1. Describe the typical organizational form (e.g., corporations, limited liability companies, etc.) and typical capitalization structure for a VC-backed Start-up in your jurisdiction (e.g., use of SAFEs, convertible notes, preferred stock, etc.). To what extent does it follow U.S. "NVCA" practice? If so, describe any major variations in practice from NVCA in your market. If not, describe whether there are any market terms for such financing VC-backed Start-ups. If venture capital is not common, then describe typical structure for a startup with investors.

Typical Corporate Entities

Many VC-backed startups in Japan incorporate as a *kabushiki kaisha* ("KK") because KKs generally help to facilitate equity financing. KKs are roughly equivalent to US-style Delaware C-corporations. Some companies instead choose to be incorporated as a limited liability company known as a *gōdō kaisha* ("GK"). GKs can be an attractive option because they do not require corporate officers (such as directors or statutory auditors), impose fewer corporate obligations, and cost less to establish. Both KKs and GKs limit shareholder liability, which poses fewer disincentives to VC funding. However, for VC-backed start-ups, KKs are more common because they provide a wider range of financing options and preserve a path to IPO. Unless otherwise noted below, these responses assume a KK entity.

Financing

Typical financing methods for VC-backed startups include: (i) issuing classes of shares that carry a preferential right to residual assets; (ii) convertible notes; and (iii) convertible equity.

At the seed stage, companies use both convertible notes and convertible equity. Issuers often structure convertible notes as "Bonds with Share Options" under Japan's Companies Act. To protect seed investors, the terms may include a conversion discount and/or a valuation cap. In Japan, one form of convertible equity – J-KISS (the Japanese version of "KISS") – is publicly available on Coral Capital's website (formerly 500 Startups Japan) – https://coralcap.co/j-kiss/.

Although Japanese investment agreements do not strictly follow the NVCA model forms, they commonly include tag-along rights and/or drag-along provisions. Japan-specific provisions also appear, perhaps the most unique of which is a representation that the parties are not affiliated with any so-called "antisocial forces" (a compliance concept aimed at excluding organized crime and similar groups).

2. Describe the typical acquisition structures for a VC-backed Start-up. As between the various main structures (including an equity purchase and an asset purchase), highlight any main corporate-law and tax-law considerations.

Typical Structures In acquisitions of VC-backed startups in Japan, buyers most commonly purchase shares (a share transfer). By contrast, parties often use a business transfer (an asset deal) when they want to acquire only a specific line of business. Because of the burdensome need to individually assign each asset and contract and obtain required consents, parties tend not to choose an asset deal when the buyer intends to acquire the entire company.

Considerations under Japan's Companies Act VC-backed startups in Japan typically issue shares subject to transfer restrictions. Therefore, any share transfer will require approval from the company's board (for companies with a board) or, otherwise, through a shareholder resolution. For business transfers involving a material part of the company's business, the Companies Act generally requires the shareholders to pass a special resolution.

Tax Considerations A share transfer does not trigger Japanese consumption tax. Individual sellers must pay a capital gains tax of approximately 20.315%. For corporate sellers, Japan aggregates the capital gains with the seller's other income and imposes corporate tax at an effective rate of roughly 30%.

Parties in a business transfer must – in addition to corporate income taxes – pay consumption tax on the taxable components of the transferred assets.

As for stamp taxes, a share transfer agreement is not taxable, whereas a business transfer agreement

constitutes a taxable document.

3. Describe whether letters of intent / term sheets are common in your jurisdiction. Are they typically non-binding or binding? Is exclusivity common? Are deposits / break-up fees common?

In Japan, parties commonly use a letter of intent (LOI) or a memorandum of understanding (MOU). An investor or acquirer typically delivers an LOI to the target company, whereas both parties enter into an MOU when setting forth their mutual understanding of the deal.

Typical LOI/MOU terms outline the main deal points, including the contemplated M&A structure, the purchase price, the seller's duty to fully cooperate with the due diligence process, specific warranties, and the expected M&A schedule. As a general rule, the parties state that the LOI/MOU is not legally binding. However, when the parties submit an LOI at the final stage of negotiations, they may designate some or all of its provisions to be legally binding.

Buyers commonly seek an exclusivity (no-shop) covenant to keep the seller from negotiating with other prospective buyers. The parties may grant exclusivity for a fixed period of time and make the exclusivity clause legally binding. In practice, to make the exclusivity binding, parties increasingly consider including a provision that allows for liquidated damages or a termination fee (a break-up fee).

4. How common is it to use buyer equity as consideration in purchasing a VC-backed Start-up? Please describe any considerations or constraints within the securities laws of your jurisdiction for using such buyer equity.

In Japan, most M&A transactions use cash as consideration, and buyers do not commonly use their own shares. However, the partial share exchange regime introduced by the 2021 amendment to the Companies Act has expanded the available options by creating a user-friendly statutory framework to use shares as consideration.

One way to use shares as consideration is for the buyer to issue its shares to the seller and receive the target shares as an in-kind contribution. However, Japan heavily regulates this option, including imposing a general requirement to appoint a court inspector to scrutinize the contribution. By contrast, the Companies Act provides buyers two ways to use their shares to acquire a company that avoid those constraints: a share exchange and a partial share exchange. A share exchange makes the target a wholly owned subsidiary of the buyer. A partial share exchange makes the target a subsidiary of the buyer.

Unlike cash deals, share-for-share transactions may require the parties to comply with domestic and foreign rules governing the issuance of shares used for consideration. If a significant portion of the target's shareholders are in the United States, U.S. securities laws – including Form F-4 registration and disclosure – may apply and discourage the use of shares as consideration. In addition, depending on the specifics of the contemplated transaction, Japan's Financial Instruments and Exchange Act (FIEA) may apply, including tender offer regulations and insider-trading restrictions. The FIEA may in certain cases also require a securities registration statement.

5. How common are earn-outs in your jurisdiction? Describe common earn-out structures, and prevalence of earn-out related disputes post-closing.

In Japanese legal practice, parties do not widely recognize or use earn-outs. Buyers and sellers nevertheless sometimes adopt them in cross-border transactions, in large deals, or in acquisitions of startups whose enterprise value is difficult to assess. Even so, the number of earn-out deals in Japan remains limited. However, practitioners recognize the flexibility and functionality of earn-outs. Because of these benefits, they expect earn-outs to expand deal feasibility and to improve efficiency and fairness when used effectively.

Parties typically base earn-out targets on financial metrics such as revenue, EBITD, net income, or other income-statement items. In practice, parties in Japan most often use EBITDA. They may also set tiered additional payments that increase with the degree to which the target meets or exceeds the parties' agreed-upon metrics.

Japan has seen disputes over how the purchase price is taxed in share transfers that include earn-out provisions.

6. Describe any common purchase price adjustment mechanisms in purchasing a VC-backed Startup and/or are lock-box structures

more common.

In standard M&A transactions, parties typically use one of the following price-adjustment mechanisms:

1. Fixed price at signing. The parties agree on a fixed amount in advance.
2. Pre-closing adjustment paid at closing. The parties adjust the price at closing to reflect any relevant changes that they identified prior to closing, (e.g., any dividends that shareholders may have received after signing but prior to closing).
3. Post-closing true-up. After closing, the parties determine and then settle any adjustment amounts based on the target's financial position on the closing date.

An earn-out can also function as a price adjustment. It modifies the purchase price after closing based on the target's performance (for example, the target's financial results) corresponding to a period that the parties have agreed on.

Adjustment items generally fall into two categories:

- Balance sheet true-ups. The parties adjust for differences between the balance-sheet items that they used as a baseline at signing and the corresponding amounts on the closing balance sheet. In practice, the most common targets are net debt, working capital, and net assets.
- Event-based adjustments. The parties adjust the price based on the occurrence or non-occurrence of specified events.

Price adjustment clauses are standard in cross-border transactions between Japanese and U.S. companies. Parties in Japan do not often use a lock-box structure, which fixes the price by reference to financial statements as of a specified date.

7. Describe how employee equity is typically granted in your jurisdiction within VC-backed Start-up's (e.g., options, restricted stock, RSUs, etc.). Describe how such equity is typically handled in a sale transaction.

Equity Incentives

In Japan, VC-backed startups typically grant stock options as an incentive to their employees. Restricted stock (RS) or Restricted stock units (RSUs), which – like stock options – deliver shares to officers and employees as compensation, are usually adopted after an IPO. This is because, if a company grants RS or RSUs while it remains private, the number of individual shareholders tends to increase, which can complicate stock-exchange listing reviews and make it more difficult to administer who can vote.

Types of Stock Options and Tax Treatment

Japanese practice recognizes several option structures, including tax-qualified stock options and paid-in-market-value stock options (stock options issued for consideration).

- If the option qualifies for favorable tax treatment, the holder does not incur any tax when exercising the stock option. Instead, the holder pays only capital-gains tax of approximately 20.315% when they sell the stock. For this reason, VC-backed startups commonly use tax-qualified stock options.
- When it is difficult or impossible to satisfy the tax-qualification requirements, companies often use paid-in-market-value stock options. The company sets the issue price at the option's fair market value and requires the grantee to pay that amount when they exercise the option and receive the stock. Here too, the exercise of the option is not a taxable event. However, grantees must make some upfront payment, which can be burdensome.

Treatment of Employee Equity Upon Acquisition

If a VC-backed startup is acquired, companies typically consider three approaches for employee-held stock options and shares:

1. **Exercise and share purchase by the buyer.** Holders of stock options will exercise their options to receive shares, and the buyer will purchase those shares. (The option grant/allotment agreement needs to specify how to handle an M&A event.)
2. **Option purchase and replacement.** The buyer will purchase the target's stock option rights from the holders and provide them with the buyer's stock option rights. (Note that this will result in lifting the non-transferability covenant, causing the loss of tax-qualified status.)
3. **Pre-agreed cancellation upon change of control.** The startup may provide in the option grant terms that, in the event of an acquisition, the startup will acquire all stock acquisition

rights without the need to provide the holder with any consideration.

8. Describe whether there are any common practices for retaining employees post-acquisition (e.g., equity grants, re-vesting of employee equity, cash bonuses, etc.).

Startups commonly adopt straightforward retention plans that condition compensation on continued service or on the target's achievement of specified performance goals. Another approach is for the acquirer to grant the target's employees stock options of the acquiring company.

In many startup M&A transactions, a key person accounts for a substantial portion of the business value. In those cases, the parties often consider providing the key person with a retention bonus and/or stock options for the acquirer's stock.

As one of the seller's post-closing obligations, the parties may prohibit the seller from encouraging the target's officers and employees – including any key individuals – to resign. These types of clauses typically include an exception for general recruiting that is not specifically directed at the target's personnel, where a target officer or employee applies on their own initiative.

9. How common are works councils / unions in your jurisdiction, among VC-backed Startups or technology companies generally?

At large enterprises in Japan – especially major corporations – employees often form both labor unions and works council-type bodies side by side. By contrast, employees at small companies (with 99 or fewer employees), including startups, rarely form labor unions.

Unlike in many European countries, Japanese law does not mandate a works council regime. Instead, unions and employers voluntarily conduct labor-management consultations, and the parties have developed cooperative labor-management relationships.

In many small and medium-sized companies that lack a union, employees still either form an internal body to represent workers or elect a representative who will engage in discussions with the employer on behalf of the employees.

10. Describe Tax treatment of founder / key people holdbacks. Are there mechanisms for obtaining capital gains or equivalent more preferable tax treatment even if continued service is a requirement for the holdback to be paid out?

1.Holdbacks as a simple installment payment of a fixed total price

If the parties have fixed the total consideration and the holdback functions as a simple installment payment of that consideration, Japan will likely* impose tax on the full purchase price as of the closing date.

- **Individual sellers:** Japan will likely tax the gain as separate capital-gains income at a rate of approximately 20.315%.
- **Corporate sellers:** Japan will likely aggregate the gain with the seller's other income for that fiscal year and impose corporation taxes at an effective rate of roughly 30%.

2. Holdback contingent on continued employment

Buyers sometimes condition payment of the holdback on the seller's continued employment.

- **Individual sellers:** Japan will likely tax as capital gains the portion of the price that is fixed as of closing (Japan's capital gains tax rate is approximately 20.315%). For the unfixed, employment-contingent portion, Japan will not treat it as capital gains eligible for separate taxation. Japan will instead likely comprehensively tax the holdback together with the individual's other income (i.e., the holdback will not qualify for the lower capital-gains rate).
- **Corporate sellers:** Japan will likely aggregate the amount with the company's other income or losses in the fiscal year when the payment becomes fixed and then impose corporate tax. As a result, the tax treatment generally does not differ from that of a simple installment payment.

*This response uses the qualifier "likely" to reflect the fact that it is not entirely certain whether Japan will impose these taxes exactly as described. Japan's National Tax Agency has not issued any official guidance on how they will tax the kind of holdbacks referenced in this question. However, based on an analysis of relevant cases and based further on common practice, it is a reasonable inference that Japan will impose these taxes as set forth in the response.

11. Describe whether non-competes / non-solicits for key employees / founders are common. Describe any legal constraints around such non-competes / non-solicits.

Founders and key employees play a critical role in many startups. As a retention tool, parties commonly use non-compete and non-solicit covenants.

Japanese law does not prohibit the parties from imposing post-termination non-compete or non-solicit obligations on founders or employees. However, Japan's constitution protects one's freedom of occupation, meaning that non-competes must remain within certain limits. Non-solicit covenants also face constraints – the parties may agree to them only to the extent that they do not constitute an unlawful tort.

Courts assess the validity of non-compete clauses by asking whether the restriction on the individual's freedom of occupation is as narrow as reasonably possible. Under this standard, Japanese practice generally considers the following to be unlawful in employment agreements between a company and its employees:

- A sweeping ban on joining a competitor without narrowing the person's prohibited duties or role;
- A non-compete duration that exceeds two years;
- The lack of a defined geographic scope; and
- A failure to provide the employee with any appropriate compensation in exchange for the non-compete restrictions.

By contrast, Japanese law has not established any clear benchmarks for determining the validity of a non-compete clause when a founder sells their shares as part of a share transfer.

12. What are typical closing conditions for the acquisition of a VC-backed Startup? How common is a "material adverse effect" concept as a closing condition?

Typical Closing Conditions

In Japanese deals involving VC-backed startups, parties typically set the following closing conditions:

1. No breach of representations and warranties.
2. Performance and compliance with covenants. By the closing date, the seller needs to have performed and complied with its obligations under the agreement.
3. Antitrust filings and waiting period. The buyer needs to have made the required share acquisition notification under the Anti-Monopoly Act, and the applicable waiting period has expired.
4. Third-party consents. The parties have obtained the required consents from counterparties to the target company's material contracts.
5. Approval of share transfer.
6. Governmental permits and approvals.
7. Cure of issues found through due diligence.

If a key person plays a critical role at the VC-backed startup, the buyer may also require the key person to remain employed as a condition to closing.

Material Adverse Effect

In Japanese M&A practice, parties commonly condition closing on the absence of a Material Adverse Effect (MAE). They often define MAE-triggering events to include, for example, a deterioration in the target company's performance or the loss of a major customer.

In recent years, parties have sometimes narrowed the MAE definition through carve-outs. Typical carve-outs exclude events that the seller cannot control, such as:

- changes affecting the overall economy or the target's industry generally;
- effects resulting from the execution or announcement of the share purchase agreement;
- changes in laws or regulations; and
- political developments or similar macro events.

13. With respect to representations and warranties: (a) Is deemed disclosure of the dataroom common? (b) Are "knowledge" qualifiers common? Is it common to make representations that are "risk shifting" (e.g., where sellers cannot completely validate the accuracy of such representations)?

a. Is deemed disclosure of the dataroom common?

Under Japanese case law, an acquirer may be barred from pursuing a claim for breach of representations and warranties if the facts underlying the claim were disclosed in the data room. To avoid that result, parties sometimes include a provision stating that, if the seller breaches its representations and warranties, the seller

will indemnify the buyer regardless of whether the buyer knew or should have known of the breach (a "pro-sandbagging" clause).

b. Are "knowledge" qualifiers common? Is it common to make representations that are "risk shifting" (e.g., where sellers cannot completely validate the accuracy of such representations)?

Sellers commonly use knowledge qualifiers. Where the seller's representations and warranties are broad in scope, the seller may wish to limit the representations and warranties by using a "to the best of seller's knowledge"-type qualifier. In that case, it is important to identify whose "knowledge" applies, specifically whether it is limited to the shareholder(s), to directors or officers seconded from a shareholder to the target company, or to the target company's directors or officers more broadly. This will affect the scope of the representations and warranties. It is also common to have the seller bear the risk of any issues that the seller itself is not aware of. For example, the seller sometimes represents and warrants that the target company is not subject to any threatened or pending litigation even though the seller cannot ascertain with complete accuracy that that statement is true.

14. Describe the typical parameters of seller indemnification, including: (a) Coverage (fundamental, specified, general reps, covenants, shareholder issues, pre-closing Tax, specific indemnities, employment classifications, etc.) (b) Liability limit (c) Survival periods

a. Coverage (fundamental, specified, general reps, covenants, shareholder issues, pre-closing Tax, specific indemnities, employment classifications, etc.)

The parties typically define indemnification coverage to include (i) breaches of representations and warranties and (ii) breaches of obligations under the share purchase agreement (including covenants).

The seller commonly represents that: (a) it has the authority to enter into and perform the agreement; (b) it has the ability to (and will) obtain internal approvals; (c) the agreement is valid and enforceable; and (d) the execution and performance of the agreement will not violate any applicable laws, court orders, or contracts. With respect to the shares being transferred, the seller typically represents that it legitimately owns the shares, that the shares are free and clear of any liens or other encumbrances, and that no impediment exists that would obstruct or prevent their transfer.

The seller's representations regarding the target company typically include that the company: (a) has a valid corporate existence; (b) is not subject to insolvency or similar proceedings; (c) has issued the number and type of shares set out in the agreement; (d) has not issued any convertible or other potential equity; (e) will not violate any laws, court orders, or contracts in connection with the execution and performance of the agreement; (f) has submitted accurate financial statements; (g) will not experience any material events after the date of the company's most recent financial statements; (h) does not have any contingent or off-balance-sheet liabilities; (i) is in compliance with all relevant laws; (j) possesses all permits and licenses necessary for the company's business; (k) is current on all its tax payments; (l) validly owns the company's material assets and that those assets are in acceptable condition; (m) is in compliance with all employment, labor, and pension matters; (n) is not subject to any threatened or pending litigation or other legal disputes; (o) is not involved in organized crime; and (p) has not experienced any changes that would materially affect the company's condition that the parties based the transaction terms on, including the purchase price.

In addition, parties sometimes "carve out" issues that they have identified in due diligence from the scope of the representations while providing a special indemnity under which the seller will specifically cover those identified risks if they materialize.

Liability limit

Parties often set a cap on indemnification to prevent the indemnifying party from bearing unforeseeable losses. Under standard market practice, parties typically set this cap at 30–50% of the purchase price. To avoid administrative burdens resulting from very small claims, parties often set a de minimis, minimum claim threshold.

Parties may exclude certain matters from the cap or from the de minimis, minimum claim threshold, including a party's breach of any "fundamental representations and warranties", i.e., matters concerning the validity of the share transfer agreement itself and the target's basic corporate attributes such as its corporate existence and the validity of its shares. Parties also often state that the cap does not apply to fraud or to a party's willful breach of the representations, warranties and covenants. Special indemnities for specified matters may likewise sit outside the cap.

Survival periods

Parties usually limit indemnification to claims made

within a set period after the closing date. They commonly agree on a claims period of approximately six months to two years.

Parties may set different survival periods depending on the subject matter of the representations and warranties. For example, parties sometimes provide an unlimited survival period for certain fundamental representations such as the target's valid existence and the seller's ownership of the shares. Parties often adopt a longer survival period for matters that they are unable to uncover even with an audit, or issues that may surface due to external factors (for example, a tax audit), and that could give rise to significant liability. This longer survival period could last seven years for tax representations and warranties, taking into account the applicable statute of limitations.

15. Describe background law that might impact the negotiation of indemnification, including those that may constrain recoverability of losses (e.g., can lost profits or multiples be awarded as damages? Is mitigation required?).

Under Japanese law, when a share transfer agreement lacks an indemnity clause, it is not always clear whether a breach of representations and warranties gives rise to a claim for damages. Accordingly, parties include indemnity provisions in share purchase agreements as a way to clarify the seller's liability for such breaches.

Under Japan's Civil Code, recoverable losses are limited to: (i) ordinary damages; and (ii) other special damages that the parties can reasonably foresee. Contracting parties often aim to expand the scope of recoverable losses by, for example, covering losses "arising out of or in connection with" the breach. Whether lost profits fall within the recoverable scope depends on the specific facts and circumstances. In practice, parties frequently draft the contract to exclude lost profits from indemnifiable losses.

The agreement should expressly provide that attorneys' fees are recoverable as damages. Without this sort of provision, courts generally do not award attorney's fees as damages.

Some case law in Japan recognizes a duty to mitigate one's damages. Parties often include an express contractual duty to mitigate damages to remove any doubt.

16. How common is Warranty & Indemnity (W&I) insurance / representations and warranties insurance (RWI)? Describe any common issues that arise in connection with obtaining such insurance for an acquisition of a VC-backed Startup. Is Tax coverage obtainable from RWI/W&I policies? Are there any common exclusions?

W&I insurance/RWI is not yet standard practice in Japan, but parties are increasingly considering it.

Parties in startup acquisitions still have limited practical experience with W&I insurance/RWI. One reason is that Japanese startups often aim for an IPO rather than M&A. Compared to more established companies, many venture companies lack robust internal controls and generally operate in a less organized manner. As a result, it may not be possible to perform an adequate level of due diligence on startups, which can lead to numerous exclusions or even an underwriter declining to provide the necessary guarantees.

W&I insurance/RWI sometimes covers tax matters. However, given the nature of tax losses and the difficulty of quantifying them, insurers often exclude them. If the insurer excludes tax-related losses from coverage, the parties may procure a separate insurance policy covering tax liability.

It is customary for W&I insurance/RWI to exclude the following categories of risk:

1. Matters that were not subject to sufficiently thorough due diligence.
2. Representation and warranty breaches that – prior to closing – the buyer either already knew about or, due to the relevant facts or circumstances, the buyer could reasonably have anticipated would lead to a breach.
3. Typical "general exclusions" such as the following: an inaccurate bring-down (no-claims) certificate; purchase price adjustment provisions in the SPA; breaches relating to projections, plans, or other forward-looking statements; civil or criminal fines, penalties, surcharges, or punitive/treble damages; bribery/anti-corruption and involvement with organized crime; product recall liability; and environmental pollution matters.

17. Briefly describe the antitrust regime in your

jurisdiction, including the relevant thresholds for filing. Describe whether there has been any heightened scrutiny of technology companies.

Japan's Antimonopoly Act prohibits M&A deals that would substantially restrain competition in a particular field of trade. If the transaction satisfies certain criteria, a purchaser will need to submit "prior notification" to the Japan Fair Trade Commission ("JFTC"). This response covers this prior notification requirement. (However, as discussed in the response to Question 18 below, Japanese law may require more than mere notification (effectively, prior approval) even when the law uses the term "prior notification.")

An acquirer of shares is required to submit prior notification if: (i) the aggregate domestic turnover in the most recent fiscal year of the acquirer's group company (which includes the acquirer itself, plus its subsidiary companies, its parent company, and subsidiaries of its parent company) exceeds JPY 20 billion, and that of the target's group company exceeds JPY 5 billion; and (ii) the acquisition results in the acquirer's group company crossing the threshold of 20% ownership of the target company or, if the acquirer already owns more than 20% of the target, crossing the 50% ownership threshold.

After the JFTC receives the purchaser's prior notification for the contemplated acquisition, the parties must generally wait at least 30 days before consummating the transaction to allow the JFTC to conduct its initial review. If the initial review results in the JFTC concluding that it needs to perform a more detailed review, the JFTC may extend the review period and conduct a secondary review.

The JFTC will assess whether the acquisition substantially restrains competition in light of various factors. These factors include the presence of powerful competitors in the market and how difficult it is for new companies to enter that market. If the JFTC determines that the acquisition will be anti-competitive, it will request the acquirer to implement remedial measures prior to the acquisition. Remedial measures include carving out and transferring part of the business, which will result in a new competitor in the market. If the acquirer fails to comply, the JFTC will issue a "cease-and-desist" order requiring the purchaser to take measures to eliminate the anti-competitive effects, including disposing of a portion of its shares in the target company.

It does not appear that the JFTC has become stricter in performing its review of M&A deals involving technology companies. However, in recent years, the JFTC has been paying increasing attention to M&A transactions that do not require prior notification, such as acquisitions of startup companies with minimal revenue. Specifically, the JFTC has recently announced a policy under which it will review acquisitions that meet the following criteria: (i) the value of the transaction exceeds JPY 40 billion; and (ii) the transaction is expected to affect domestic customers. The JFTC further recommends that the acquirer involved in such transactions consult with the JFTC beforehand to ensure that the acquisition will not have any anti-competitive effects.

18. Briefly describe the foreign direct investment regime in your jurisdiction, including the relevant thresholds for filing. Describe whether there has been any heightened scrutiny of technology companies.

As discussed above in the response to Question 17, the FEFTA will generally require a foreign investor to submit so-called "prior notification" to the authorities when directly investing in a Japanese company that is engaged in one or more designated business sectors. Although the law uses the term "notification" for these transactions, this procedure in effect functions as a prior approval regime because investors can commence transactions only after they obtain clearance from the authorities. This response will therefore use the term "prior approval" to avoid confusion. The term "designated business sectors" broadly includes the manufacturing of information-processing equipment, components and software, and information services-related industries. In recent years, the authorities have gotten stricter in the technology sector by adding sectors such as semiconductors, advanced electronic components, industrial robots, and storage batteries.

Prior approval will be required even if the foreign investor acquires the shares through a Japanese subsidiary or where the investor indirectly holds the shares through a custodian. Moreover, the FEFTA will consider the acquisition of even a single share of an unlisted Japanese company to be "directly investing in a Japanese company," so investment in a VC-backed startup that is involved in a designated sector will typically require prior approval.

The earliest the investor is allowed to submit its request for prior approval is six months prior to the intended closing date (they are not allowed to submit it any sooner). The foreign investor must then wait at least 30 days after submitting its request before it can proceed with the transaction. The government may extend the review period by up to five months.

Even if a foreign investor does not need to obtain prior approval for a deal that does not fall under one of the designated business sectors, they must nevertheless submit a post-investment notification no later than 45 days after the acquisition.

19. Briefly describe any other material regulatory regimes / approvals that may apply in the context of an acquisition of a technology company.

Japan has no sector-specific regulations unique to the acquisition of technology companies. However, if one or more Japanese laws require the target company to hold certain licenses or authorizations, those laws may require the target company to notify the relevant authorities of any changes in the target company's shareholders. To cite just one example, a company that provides funds transfer services (excluding banks) must notify the local finance bureau and submit an updated shareholder list when there are changes to its major shareholder, which is a person or entity that holds 10% or more of the company's voting rights.

20. Briefly describe any common issues that arise with respect to intellectual property, in the context of an acquisition of a technology company.

The acquirer should confirm whether the target company rightfully owns its intellectual property (IP), including their patents, trademarks, copyrights, and know-how. The acquirer should also ascertain whether the target company co-owns any IP with third parties or if the target company is a party to any existing licensing arrangements with third parties. In particular, the lack of clear contractual provisions often makes it unclear who owns the IP where the IP arises from employee inventions or works, joint development/authorship, or outsourced projects. This uncertainty may make it difficult or even impossible for the target company to enforce its IP rights and to commercially benefit from the IP after the acquisition.

The acquirer should also verify that any registered patents and trademarks are valid, that they are broad enough in scope to allow the target company to continue operating its business, and that there is no risk of IP-related legal disputes. Moreover, the acquirer should pay attention to unpatented (unregistered) technologies and know-how, and ensure that the target company adequately maintained an appropriate level of confidentiality over those technologies and know-how.

The acquirer should investigate whether the target company's products or services infringe any third-party IP, and whether the target company has put in place sufficient mitigation measures (such as cross-licenses), particularly in relation to standard-essential or other essential patents.

For technology and software that third parties have licensed to the target company, the acquirer should review the license agreements to confirm that the target company can continue to use them after the acquisition and whether any restrictions (such as change-of-control clauses) may apply.

21. Briefly describe the regulatory regime for data privacy in your jurisdiction and highlight any common issues that arise in the context of an acquisition of a technology company.

Japan's Act on the Protection of Personal Information (APPI) provides Japan's cross-sector data privacy framework, with the Personal Information Protection Commission (PPC) acting as the supervisory authority. If a business operator violates the APPI, the PPC may exercise its powers, including requesting information from the business, conducting on-site inspections, and issuing guidance, advice, recommendations, and orders. If the business operator fails to follow a PPC order, it may face criminal penalties, including fines.

Japan does not have an EU-style administrative surcharge (penalty) regime.

Pre-Closing Due Diligence: Because Japan's APPI restricts a third-party from providing an individual's personal data without that individual's consent, parties generally anonymize personal data of the target company's officers and employees prior to uploading that personal data to the data room.

Post-Closing Transfers: After the share acquisition, the acquirer must typically obtain the individual's consent in order for the target company to legally transfer the individual's personal data to the acquirer.

Cross-Border Transfers: When a foreign acquirer receives personal data from the target company, Japanese law may apply additional requirements compared to a domestic transfer. If the target company provides personal data to a third party in a foreign country (which, in the context of an M&A transaction, is the acquirer), the target company must provide the individual with certain information, including: (i) a description of the foreign jurisdiction's personal data protection regime; and (ii) the

safeguards that the foreign recipient will implement to protect the individual's personal data. The target company must then obtain the individual's consent to the cross-border transfer. The target company is not required to take this additional step when transferring an individual's personal data to an acquirer located in a country specified under the European Economic Area framework.

22. Briefly describe any common issues that arise with respect to employment laws, in the context of an acquisition of a technology company (e.g., contractor misclassification).

In a share transfer, the target company remains the employer. As a result, the employment relationship itself usually continues without major issues.

However, startups are often less aware of compliance issues compared to more established companies. For this reason, it is not rare for startups to encounter labor law compliance problems. A frequent issue is that startups fail to provide their employees with the legally required overtime pay. If due diligence identifies any unpaid overtime, parties may reduce the purchase price or require the seller to indemnify the purchaser for any overtime-related liability.

Individual labor disputes can also affect indemnities and other risk allocations. These disputes include harassment claims or cases of wrongful termination.

If the target company has a labor union, a labor-management agreement may require the target company to consult with the union before proceeding with the M&A deal. Even if no such agreement exists, the parties should consult with the union to minimize any employment issues.

If the target company has agreements with individual contractors, the acquirer should verify that those contractors do not, in substance, constitute employees. In this connection, if the contractors are subject to the target company's direction and control, they may be deemed employees under Japanese law. In that case, the target company may owe those contractors overtime based on how many hours they actually worked, and it may be difficult for the target company to terminate the contract.

Even when the target company outsources work to a company, the acquirer should pay close attention to that company's employees. If the target company directly directs and supervises the other company's employees, the arrangement may constitute an illegal worker dispatch under Japan's Worker Dispatch Act. In some cases, the law may deem an employment contract to exist between the target company and those employees, which, again, can make it difficult for the target company to terminate the employees.

23. Briefly describe any recommendations for dispute resolution mechanisms for M&A transactions in your jurisdiction and highlight any common issues that arise in the context of an acquisition of a technology company.

In cross-border transactions, the parties often agree to arbitration rather than to court litigation. Arbitration offers the following advantages: (i) the parties can more quickly resolve disputes because – unlike in court – the losing party is unable to appeal; (ii) the parties can select the arbitrators, which enables the appointment of subject-matter experts and a more robust evidentiary process; and (iii) hearings are not public, which helps protect confidentiality in disputes involving sensitive information (tech companies frequently choose arbitration for this confidentiality benefit).

Japan is a contracting state to the New York Convention. Accordingly, even if the seat of arbitration is outside of Japan, a party will be able to enforce the arbitral award in Japan.

To facilitate arbitrations seated in Japan, recent amendments to Japan's Arbitration Act introduced, among other things, the following changes: (i) a new regime allowing Japanese courts to enforce interim measures ordered by an arbitral tribunal (i.e., measures to preserve evidence or a party's rights pending the final award); and (ii) when seeking an order from a Japanese court to enforce an arbitral award (an enforcement decision), the party does not need to attach a Japanese translation of the award if the court deems the translation unnecessary.

24. Briefly describe any special corporate or stamping formalities that transaction parties should make sure to plan for in your jurisdiction (notarization, etc.).

If the target company's shares are subject to any transfer restrictions, the acquirer must obtain approval from the target company's shareholders or its board of directors, as applicable. To make the transfer enforceable against the target company, the target company must change the

entry in its shareholder registry from the seller to the acquirer. The share purchase agreement should require the seller to take all actions necessary to obtain the approval and to ensure that the seller updates its shareholder registry.

No notarization is required for a share acquisition.

A share purchase agreement prepared in Japan generally does not constitute a taxable document under Japan's Stamp Tax Act. Therefore, the parties do not need to affix a revenue stamp if the agreement contains only provisions relating to a standard share transfer.

In some cases, the share purchase agreement also governs transactions other than the share transfer, e.g., some provisions may create an ongoing commercial relationship between the seller and the acquirer after closing. If so, the agreement may constitute a taxable document in relation to those other transactions. If the parties prepare the agreement as a PDF instead of a hard copy original, the parties will not need to affix a revenue stamp to the agreement.

Documents that a party delivers at closing may require revenue stamps. For example, (i) the acquirer is required to affix a revenue stamp to the receipt that it provides to the seller for receiving the seller's share certificates at closing, and (ii) the seller is required to affix a revenue stamp to the receipt that it provides to the acquirer evidencing the purchase price that the acquirer paid.

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