



Recent Developments in Court Decisions on Poison Pills in Japan



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A. Introduction

In recent years, the number of cases of hostile takeovers has increased in Japan, and more and more listed companies are trying to introduce, maintain or renew hostile takeover defense measures. Since the spring of 2021, important court decisions have been made on such hostile takeover defense measures, and this article discusses the latest trends in these court decisions.

B. Typical Scheme of a Poison Pill in Japan

At present, the poison pill generally used in Japan is called the “advance-warning type takeover defense measure.” The typical design features of this poison pill are as follows:

- Before starting a bulk purchase of a certain percentage or more of the shares of a target company, the acquirer is required to (a) agree with the target company to follow certain procedures stipulated in the defense measure, and (b) provide certain information on the acquisition to the board of directors of the target company.
 - After the information is provided by the acquirer, the target company will consider whether or not the acquisition is appropriate from the perspective of the expected benefit to its shareholders, and as a result of such consideration, the opinion of the board of directors of the target company will be announced. During this review period, the acquirer will not be able to initiate the bulk purchase of the shares of the target company.
 - If the acquirer does not follow these rules, then the target company will invoke the countermeasure.
 - The countermeasure is the gratis allotment of stock options. The stock options are designed as follows: (a) the acquirer and its related parties cannot exercise the stock options (i.e., discriminatory exercise conditions), and (b) if the target company acquires the stock options, then common stock will be delivered to the shareholders other than the acquirer and its related parties, but cash or other stock options with different conditions will be delivered to the acquirer and its related parties (i.e., discriminatory acquisition clauses).
 - If such countermeasure is invoked, then the shareholding ratio held by the acquirer and its related parties will decrease, resulting in a takeover defense effect.
- In the past, most companies have obtained the approval of the shareholders in the form of a voluntary resolution at a general meeting thereof to introduce an advance-warning type takeover defense measure during peacetime. However, in recent years, there has been an increasing number of cases wherein takeover defense measures are introduced or renewed in cases of an emergency, that is, when the threat of a hostile takeover has materialized.



Other features of recent takeover defense measures are:

- In many cases, the takeover defense measure is designed to target a specific acquirer (“**Specific Target Type**”).
- In some cases, the measure is introduced only by a resolution of the board of directors, without holding a general meeting of the shareholders, because of an emergency.
- When invoking a countermeasure based on a takeover defense measure (i.e., gratis allotment of stock options), it is customary to schedule the passing of a resolution at a general meeting of the shareholders to confirm the majority view of the shareholders.

C. Recent Cases on Poison Pills

a. Toshiba Machine Case

Toshiba Machine Co., Ltd. (currently, Shibaura Machine Co., Ltd) (“**Toshiba Machine**”) had introduced an advance-warning type takeover defense measure; however, immediately after abolishing it, City Index Eleven (“**CI11**”), a Japanese activist, announced its intention to make a hostile tender offer for the shares of Toshiba Machine. In response, Toshiba Machine introduced a Specific Target Type takeover defense measure.

The takeover defense measure of Toshiba Machine was a poison pill that required compliance with certain procedures only by CI11 and its related parties, the specific large-scale purchasers who have already been identified in the emergency. It is said to be the first poison pill in Japan to have such characteristic as a Specific Target Type takeover defense measure.

In this case, CI11 withdrew its tender offer, and therefore, no countermeasure was invoked and no court ruling was made.

b. NIPPO Case

Unlike the Toshiba Machine Case, the court made a decision in this case on the implementation of a Specific Target Type takeover defense measure.

NIPPO Ltd. (“**NIPPO**”), a Japanese manufacturer, has been approving the renewal of its takeover defense measure at the general meeting of the shareholders for several years. Freesia Macros, a Japanese manufacturer, tried to purchase a large amount of NIPPO’s stock without following the information provision rules stipulated in the said measure. In response, NIPPO implemented a countermeasure (i.e., gratis allotment of stock options) just by passing a board resolution.

Freesia Macros then filed for a provisional disposition of an injunction against the gratis allotment of stock options with the Nagoya District Court. The petition was granted by the said court. However, another body at the Nagoya District Court and the Nagoya High Court overturned the above decision of the district court, and the petition for a provisional injunction was ultimately denied. The latter courts emphasized the fact that the introduction and renewal of NIPPO’s defense measure were approved by the shareholders based on the specific risk of a hostile takeover by Freesia Macros even though the stock options were granted by a board resolution only.

c. Japan Asia Group Case

After CI11 failed to acquire Toshiba Machine, CI11 announced the start of a hostile tender offer following the purchase of a large amount of shares in Japan Asia Group Limited (“**Japan Asia Group**”), which is a holding company of environment-related businesses. In response, Japan Asia Group introduced a poison pill with almost the same scheme as that of Toshiba Machine, but only through a board resolution, and thereafter decided the gratis allotment of stock options pursuant to such poison pill on the basis again of only a board resolution without holding any general



meeting of the shareholders.

CI11 then filed for a provisional disposition of injunction against the gratis allotment of stock options with the court. The motion for a provisional injunction was granted not only at the court of first instance but also at the appeals court. In response to the court decisions, Japan Asia Group canceled the gratis allotment of stock options, and CI11 started and eventually succeeded in the tender offer that had been announced.

In this case, the poison pill, as a general rule, required the approval of the general meeting of the shareholders before the countermeasure can be invoked. However, the poison pill exceptionally allowed the board of directors to invoke the countermeasure without a shareholder's approval in case of a large-scale purchase that violates the rules stipulated by the poison pill. Thus, the countermeasure can be invoked even only by a board resolution under such exceptional circumstance, without it having to be reviewed or ratified at a shareholders' meeting. Such exceptional mechanism of the poison pill was thus considered to be the major factor in the court decisions invalidating the said poison pill and granting CI11's motion for a provisional injunction.

d. Fuji Kosan Case

Aslead Capital Pte. Ltd. (“**Aslead**”), a Singapore-based investment firm, launched a hostile tender offer against Fuji Kosan Co., Ltd. (“**Fuji Kosan**”). In response, Fuji Kosan introduced a takeover defense measure with almost the same scheme as that of Japan Asia Group based only on a board resolution, and invoked the countermeasure based solely on a separate board resolution.

Aslead filed for a provisional disposition of injunction against the gratis allotment of stock options with the court, but neither the Tokyo District Court nor the Tokyo High Court granted the motion for an

injunction. Aslead then withdrew the tender offer, and Fuji Kosan canceled the gratis allotment of stock options.

The poison pill in this case had a characteristic that was different from the defense measure of Japan Asia Group. Even if the countermeasure was once invoked by a board resolution, a general meeting of the shareholders was required to be held before the gratis allotment of stock options was to become effective, and if the invocation is not approved at the general meeting of the shareholders, then the gratis allotment will be suspended. In this case, the invocation of the countermeasure was approved by an extraordinary general meeting of the shareholders. Due to this characteristic of the poison pill and the subsequent shareholders' approval, the countermeasure of Fuji Kosan was judged to be legal.

e. Tokyo Kikai Seisakusho Case

This case is important because the Supreme Court issued a decision on the legality of a Specific Target Type takeover defense measure.

Asia Development Capital Co. Ltd. (“**ADC**”), a Japanese investment company, bought a large number of shares in Tokyo Kikai Seisakusho, Ltd. (“**TKS**”) on the market. In response, TKS introduced a takeover defense measure with a scheme that is almost similar to that of Toshiba Machine based only on a board resolution, and invoked the countermeasure based solely on a separate board resolution.

ADC then filed for a provisional disposition of injunction against the gratis allotment of stock options with the court, but neither the Tokyo District Court nor the Tokyo High Court granted the motion for an injunction. ADC then appealed to the Supreme Court, which, however, supported the Tokyo High Court's decision. Further, prior to the Supreme Court's decision, TKS received ADC's written pledge that ADC would reduce its shareholding ratio in TKS to



32.72% (which was the threshold for invoking the countermeasure) or less, and therefore, TKS suspended the granting of the stock options.

Under this poison pill, if the invocation of a countermeasure is not approved by a majority of the votes of the attending shareholders with voting rights, excluding ADC and its related parties, and the TKS's directors and related parties (i.e., majority of the minority), at the general meeting of the shareholders (the "**MOM Resolution**"), then the gratis allotment of stock options will be suspended. In this case, the MOM Resolution was obtained at the general meeting of the shareholders held after the filing of the petition for a provisional disposition of injunction, and this point is considered to be one of the major factors in the court's ruling that held that the defense measure in this case was legal.

D. Conclusion

As far as the recent court decisions on takeover defense measures are concerned, it seems important to obtain the approval of the shareholders at the general meeting thereof to introduce and invoke a valid takeover defense measure. Moreover, in designing takeover defense measures, it is essential that at least a general meeting of the shareholders is scheduled to be held if the countermeasure is to be invoked.