

Japan Corporate & Finance Insights

Proposed Revision to the Exemption from Making Prior Notification in connection with Foreign Direct Investment

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I. Summary

Revisions are planned to existing regulations related to the Cabinet Order and Ministerial Ordinances, etc. (collectively, the “**Ordinance**”) under the Foreign Exchange and Foreign Trade Act (“**FEFTA**”) with respect to foreign investment in, or the taking of certain corporate actions with respect to, Japanese companies. The Ordinance’s proposed revisions include:

- A) Adding “Specified Foreign Investors” and “Quasi-Specified Foreign Investors” as new categories of foreign investors.
- B) “Specified Foreign Investors” are expected to be defined as foreign investors who are obligated to cooperate with foreign governments and, as a result, will need to disclose certain information to foreign governments. This new category of foreign investors will not be permitted to take advantage of the existing exemption from making prior notification to relevant Japanese ministries for any direct investments in Japanese companies engaged in “Designated Business Sectors”¹ in Japan.
- C) “Quasi-Specified Foreign Investors” are expected to be defined as foreign investors who are deemed equivalent to “Specified Foreign Investors”. For direct investments made in “Core Sectors”² other than “Designated Core Business Entities” made by these foreign investors, “Quasi-Specified Foreign Investors” will be able to utilize the exemption from prior notification, although it will be required to comply with new additional conditions when using the exemption. Furthermore, the proposed revision plans to add “Designated Core Business Entities” as a new category of Japanese companies, and a foreign direct investment in “Designated Core Business Entities” by Quasi-Specified Foreign Investors will not be exempt from the prior notification system.

II. Current Prior Notification System for Foreign Direct Investment

a. Foreign Direct Investment in Japan Requiring Prior Notification

Under the FEFTA regime, when foreign investors make an investment in or take certain corporate actions with respect to Japanese companies, a foreign investor must submit either a prior notification or a post-

¹ Designated Business Sectors have been designated in a public notice issued by the Ministry of Finance of Japan (the “**MOF**”) and Competent Ministries pursuant to the Ordinance. They include business sectors that relate to the national security of Japan, the maintenance of public order in Japan and the protection of the Japanese public (collectively referred to as “**Japan’s National Security, etc.**”).

² Core Sectors are specific industries out of the Designated Business Sectors designated in a public notice, also issued by the MOF and Competent Ministries pursuant to the Ordinance, as having a significant impact on Japan’s National Security, etc.

investment report to the relevant Japanese ministry having jurisdictional oversight of the Japanese investee company's business. As used herein, these investments in or actions are referred to as "**FDI**".

Prior notification is required by foreign investors in connection with FDI if the Japanese investee company, including in some cases its subsidiaries, operates in one or more Designated Business Sectors.

As used within this prior notification system, the concepts of foreign investors include corporations and entities formed under foreign law and regulation; investment in a Japanese company means acquiring 1 percent or more of the shares of a listed company or acquiring any shares of an unlisted company (no threshold); and Designated Business Sectors include, but are not limited to, weapons, aircraft, nuclear facilities, space-related, semiconductors, dual-use goods, cybersecurity-related, electric power generation, other critical infrastructure and important health/life sciences.

b. Exemption from Making Prior Notification

However, if foreign investors comply with certain conditions, then they are exempt from making a prior notification in connection with a FDI transaction.

The outline of the current prior notification exemption system is as follows.

○ **Exemption Conditions (highlighted in blue in chart 1):**

For FDI that otherwise requires a foreign investor to submit a prior notification, an exemption from making this submission is available in the following circumstances:

- When foreign financial institutions³ acquire 1 percent or more of the shares of a listed Japanese company.
- When foreign investors (other than foreign financial institutions which acquire shares of a listed Japanese company and foreign investors which are disqualified from using the exemption because of, among other things, having previously been sanctioned for a FEFTA violation⁴) acquire shares of Japanese companies that do not operate in Core Sectors, regardless of whether the investee company is listed or unlisted.

When relying on this exemption scheme, foreign investors must comply with the following three conditions:

³ Foreign financial institutions are required to be subject to regulations under financial regulatory laws in or subject to supervision in Japan or in other jurisdictions that have equivalent regulatory laws as Japan.

⁴ Such foreign investors hereinafter referred to "**Disqualified Investors**".

- (i) Investors or their closely-related persons will not become board members or corporate auditors of the investee company.
- (ii) Investors will not propose to the general shareholders' meeting of the investee company a transfer or other disposition of its business activities in Designated Business Sectors.
- (iii) Investors will not access non-public information about the investee company's technology in relation to its business activities in Designated Business Sectors.

○ **Additional Conditions (highlighted in orange in Chart 1):**

When foreign investors acquire 1 percent or more shares of a listed Japanese company operating in a Core Sector and the investment ratio and voting rights ratio after such shares acquisition are less than 10 percent, together with those of closely related parties to the acquiring foreign investors, two further conditions apply in addition to compliance with the three conditions listed above:

- (iv) Investors will not attend meetings of the investee companies' executive board or committees that make important decisions with respect to their activities in Core Sectors.
- (v) Investors will not make proposals, in written form, to the executive board of investee companies or board members with respect to their activities in Core Sectors that require responses and/or actions by the executive board or board members by certain deadlines.

○ **Entities Unable to Use the Exemption (highlighted in yellow in Chart 1):**

Foreign governments, foreign government-owned companies, and Disqualified Investors may not use the prior notification exemption scheme.

【Chart 1】(In the case of acquiring 1 percent or more of the shares of a listed company)

Investee's business	Type of Foreign Investors	Foreign financial institutions	General investors	<ul style="list-style-type: none"> • Foreign governments • Foreign government-owned companies • Disqualified Investors
	Non-Designated Business Sectors	No prior notification is required		

Designated Business Sectors other than Core Sectors	Exemption from prior notification available only when complying with exemption conditions			
Core Sectors ⁵		Less than 10%	10% or more	
		Exemption available only when complying with exemption conditions + additional conditions	Prior notification required Exemption not available	

III. Proposed Revision to Exemptions

The proposed revision to the Ordinance plans to add "Specified Foreign Investors" and "Quasi-Specified Foreign Investors" as new categories of foreign investors. Additionally, "Designated Core Business Entities" is expected to be added as a new category of Japanese companies.

The red-font text in Chart 2 indicates the new items that are planned to be added.

【Chart 2】(In the case of acquiring 1 percent or more of the shares of a listed company)

Type of Foreign Investor	Foreign financial institution	General investors	Quasi-Specified Foreign Investors	<ul style="list-style-type: none"> • Foreign governments • Foreign government-owned companies • Disqualified Investors • Specified Foreign Investors
Investee's business				
Non-Designated Business Sectors	No prior notification is required			

⁵ In the case of Core Sectors, the exemption is not available for the acquisition of shares of an unlisted company.

Designated Business Sectors other than Core Sectors	Existing Exemption Conditions				Prior notification required Exemption not available
Core Sectors ⁶		Existing Exemption Conditions + Existing Additional Conditions ⁷	Less than 10%	10% or more	
Designated Core Business Entities			Exemption available by compliance with further additional conditions	Prior notification required Exemption not available	

a. Specified Foreign Investors

Foreign investors which fall under either of the following categories will be regarded as “Specified Foreign Investors” under the proposed revision:

1. Organizations or individuals who have obligations to cooperate with foreign governments, etc. in collecting information that is highly likely to undermine Japan’s National Security, etc. based on agreements with those foreign governments or under foreign laws and regulations.
2. Organizations controlled by foreign investors referenced in the preceding item or by foreign governments, etc. which impose obligations on these investors. This control may be established through:
 - a. 50 percent or greater ownership of the voting rights or shares of the relevant organizations; or
 - b. by the appointment of one-third (1/3) or more of the relevant organization’s officers.

Organizations of the type described in item no. 1 are referred to as “Obligated Information Collectors,” while organizations that fall within both nos. 1 and 2 together are referred to as “Obligated Information Collectors, etc.”

⁶ In the case of Core Sectors, the exemption is not available for the acquisition of shares of an unlisted company.

⁷ In the case of Core Sectors, the exemption is not available for the acquisition of 10% or more of shares of a listed company.

Specified Foreign Investors will not be allowed to use the prior notification exemption scheme for FDI in any Designated Business Sector.

It may be useful to discuss the concept of Specified Foreign Investors in the context of specific foreign law. For example, Article 7 of the National Intelligence Law of the People's Republic of China states, "Any organization or citizen shall support, assist and cooperate with the state intelligence work in accordance with the law, and keep the secrets of the national intelligence work known to the public."⁸ Although the definition of "organization" under Chinese law is unclear, it is likely that companies registered in the People's Republic of China are included within the concept of an "organization". Additionally, under Article 33 of the Constitution of the People's Republic of China, "All persons holding the nationality of the People's Republic of China are citizens of the People's Republic of China."⁹ Therefore, it is likely that individuals holding Chinese nationality are included in the "citizen" concept. Accordingly, if Article 7 of the National Intelligence Law is interpreted as imposing an obligation on an "organization" and a "citizen" to cooperate with the state intelligence work, it can be understood that companies registered in China and individuals holding Chinese nationality have a legal obligation to cooperate with a foreign government in collecting information. However, the breach of the obligation under this Article 7 is not subject to penalty as long as the "organization" or "citizen" does not "interfere with" intelligence work. Therefore, there may be an interpretation that this Article 7 is a declarative clause and not a legally enforceable obligation.

Thus, depending on how the concept of "information that is highly likely to undermine Japan's National Security, etc." is actually defined in the revision of the Ordinance when finally adopted and how one interprets the National Intelligence Law of the People's Republic of China, it is possible that Chinese companies and their subsidiaries could be included within the concept of "Obligated Information Collectors, etc." as described earlier. As such, these foreign investors will not be able to avail themselves of the exemption from prior notification in connection with FDI in any Designated Business Sector.

In addition, since organizations or individuals who have the obligations to cooperate with foreign governments, etc. based on agreements also fall under "Obligated Intelligence Collectors", not only Chinese companies and their subsidiaries, but also organizations and individuals bound by such obligations based on agreements may be included within this category that cannot use the prior notification exemption.

Finally, if one-third (1/3) or more of an organization's officers have obligations to cooperate with foreign governments, etc., then the organization having such officers also be an "Obligated Information Collectors, etc." and not able to rely on the exemption. Therefore, it is advisable to confirm if the officers have such

⁸ English translation taken from https://cs.brown.edu/courses/csci1800/sources/2017_PRC_NationalIntelligenceLaw.pdf

⁹ English translation taken from http://www.npc.gov.cn/zgrdw/englishnpc/Constitution/2007-11/15/content_1372964.htm

obligations as well in the selection of officers, depending on the final terms of the revision.

b. Quasi-Specified Foreign Investors

Foreign investors which fall within any of the following three categories are planned to be regarded as “Quasi-Specified Foreign Investors” under the proposed revision, even if they otherwise will not be regarded as “Specified Foreign Investors”:

1. Their substantive decision-making is controlled by Obligated Intelligence Collectors, such as where (a) a minority of their officers who are Obligated Intelligence Collectors control their decision-making or (b) Obligated Intelligence Collectors take control of the decision-making by threats.
2. Their substantive headquarters are located in foreign countries or regions other than the countries or regions of their incorporation/formation, and their activities are affected by the laws and regulations of such other countries or regions regarding information collection activities.
3. Investors with the obligations to cooperate with foreign governments in collecting information based on agreements with Obligated Information Collectors, etc. or with organizations or individuals that has entered into such an agreement (including each agreement when having chains of similar agreements).

Furthermore, the proposed revision plans to add “Designated Core Business Entities” as a new category of Japanese companies, and FDI in “Designated Core Business Entities” by Specified Foreign Investors or Quasi-Specified Foreign Investors will not be eligible for the prior notification exemption system.

The proposed revision related to Quasi-Specified Foreign Investors is as follows:

- A) For FDI in Designated Business Sectors by Quasi-Specified Foreign Investors, the existing exemption conditions will be applied (the blue category in Chart 2).
- B) For FDI in Core Sectors by Quasi-Specified Foreign Investors, further conditions in addition to the existing three exemption conditions and two additional conditions will be required in order for the exemption to be available (the orange category in red-line font in Chart 2 plus the additional conditions described below).
- C) For FDI in the new category of Designated Core Business Entities by Quasi-Specified Foreign Investors, the use of the prior notification exemption will not be available (the yellow category in red-line font in Chart 2).

The further additional conditions noted in item B) above are as follows:

- a. The foreign investors shall not access non-public information about Core Sectors in which the investee company is active (however, such investors may have access to information about the investee company's officers and financial condition), and
- b. The foreign investors shall not dispatch employees to investee companies and shall not recruit or solicit officers or employees of investee companies.

The additional condition contemplated in a. above expands the prohibition of access to non-public business information broadly, beyond the existing condition (iii) under "II. Current Prior Notification System for Foreign Direct Investment -- Exemption Conditions" above that currently prohibits access to an investee company's non-public technical information.

The additional condition contemplated in b. above adds further restrictions by prohibiting the seconding of employees to, as well as the recruitment or solicitation of officers or employees of, investee companies, in addition to the existing condition (i) under "II. Current Prior Notification System for Foreign Direct Investment -- Exemption Conditions" above that currently prohibit foreign investors from assuming director or corporate auditor positions.

With regard to C) above, Designated Core Business Entities are planned in the revision to be categorized as "Specified Essential Infrastructure Service Providers"¹⁰ that conduct business activities in Core Sectors. As a new category of Japanese companies, Quasi-Specified Foreign Investors may need to verify whether the investee can be characterized as being a Designated Core Business Entity.

IV. Practical Implications

If the proposed revision to the prior notification exemption scheme is adopted, the exemption will not be available and prior notification to the competent Ministry will be required in the following FDI transaction types:

- Acquisitions by Specified Foreign Investors of 1 percent or more of the shares of a listed Japanese company that is engaged in one or more Designated Business Sectors;
- All acquisitions by Specified Foreign Investors of shares of an unlisted Japanese company that is engaged in one or more Designated Business Sectors; and

¹⁰ Article 50, Paragraph 1 of the Economic Security Promotion Act through Integrated Implementation of Economic Measures. "Specified Essential Infrastructure Service Providers" are entities which fall under the criteria provided by order of the competent ministry as conducting certain specified essential infrastructure business (a business such as the production or provision of electricity or gas, etc. specified by a Cabinet Order as providing services that form the basis for the lives of the citizenry or economic activity and for which disruption that affects their stability is likely to cause damage to the security of the nation and its citizens) for which suspension or degradation of the function of the specified critical facilities in use are highly likely to cause damage to the security of the nation and its citizens.

- Acquisitions by Quasi-Specified Foreign Investors of shares of a Designated Core Business Entity (for listed companies, only acquisitions of 1 percent or more of shares are applicable).

In February 2025, the specific articles of proposed revision to the Ordinance under FEFTA were published, and a public comment process was conducted.¹¹ The results of the public comments are now awaited, to be followed by final adoption of the revision.

As the revised articles of the Ordinance may be adjusted in response to the public comments or there may be supplemental explanations provided as to the terms of the revision, it is necessary to closely monitor what the Government does as it moves the Ordinance's revision process forward.

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If you have any questions regarding the matters covered in this memorandum, please reach out to your usual TMI contact or the attorneys listed above.

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¹¹ <https://public-comment.e-gov.go.jp/pcm/detail?CLASSNAME=PCMMSTDETAIL&id=395122504&Mode=0>