ACGA Statement on Third-Party Allotments in Japan

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Recent events in the Japanese corporate sector have once again highlighted weaknesses in the system regulating third-party allotments (private placements) and their potential adverse impact on minority shareholders. Specifically, ACGA and its investor members, many of whom are active participants in the Japanese markets, have serious concerns about the use of large third-party allotments, and believe greater scrutiny by Japanese financial regulators is needed to ensure that these transactions are carried out more fairly and transparently.

As ACGA has previously pointed out in our "White Paper on Corporate Governance in Japan (2008)" and "Statement on Corporate Governance Reform in Japan (2009)", issuing shares for cash to a select group of investors through a third-party allotment is potentially unfair to shareholders not invited to participate. Depending on how market prices move, they can suffer dilution from both the new shares issued and the discount at which they are issued. It can also abruptly change the ownership structure of the issuing company. For this reason, both regulations and best practices have evolved in other global markets that put tight restrictions on such issuances. These include:

- Shareholder approval of mandates that allow directors to place new shares at any time within the following 12 months.
- A limit on the amount of new shares that can be issued (as a percentage of existing share capital) to 5-10% or less in any 12-month period.
- A 5-10% limit on the discount at which the new shares can be issued.

However, the listing rules of the Tokyo Stock Exchange (TSE) do not require companies to seek annual shareholder approval for third-party allotments, while allowing them to issue up to 25% of existing share capital. If a company were to take full advantage of the current rules, this means it could bring in a new major shareholder who would have a decisive say on management without any input from other existing shareholders. That clearly would be adding insult to their injury from potential dilution.

We believe a mandatory annual renewal of shareholder approval for third-party allotments is critical for the equitable treatment of all shareholders, and necessary for the protection of the interests of minority shareholders.

Many listed Japanese companies have taken up the cause of corporate governance reform in recent years. However, the current system of third-party allotments in Japan is against the spirit of good corporate governance, and most investors would not look favourably upon companies that continue to exploit it. We urge Japanese authorities to consider a stronger regime governing such capital-raising transactions.

Asian Corporate Governance Association

The Asian Corporate Governance Association (ACGA) is a Hong Kong-based independent membership organisation dedicated to promoting corporate governance in Asia. ACGA covers 11 markets in the region and facilitates improvements through research, advocacy and educational programmes. It is Asia's leading expert organisation on corporate governance.

ACGA's membership comprises major global pension funds and asset managers that manage US$10 trillion in assets, as well as highly regarded Asian listed companies, intermediaries and tertiary institutes.

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