

# Listing Examination

## (Criteria for Listing Examination of Stock, Article 5)

Eligible applicant satisfying listing criteria stated in Chapter II will be examined in terms of following points: 'Appropriate Disclosure of Corporate Profile and Risk Information', 'Sound Corporate Management', 'Subsidiary Listing Rules' and 'Other Items in the Public Interest and Investor Protection'. Some of the questions TSE's examiners will be asking in the course of examination are listed in 'Interview Questions' (Please see page 39.)

Examination will cover applicant and its Affiliated companies in their corporate group.

(Note) 'Affiliated companies' means any person-related companies (those that are related with applicant by HR, funds, technology, transactions, etc., and either their management is controlled by applicant, or applicant's management is controlled by them) or capital-related companies (either applicant (including its person having special relationship) owns 20/100 or more voting right of them, or they own 20/100 or more voting right of applicant) that has been controlled or owned by the applicant or those companies that control or own the applicant.

### **1 Appropriate Disclosure of Corporate Profile and Risk Information (CLES: Art.5-1(1))**

Applicant will be examined whether they are able to follow disclosure laws and regulations (CLES: Art.5-1(1)). They need to meet following requirements:

(1) Corporate profile information disclosure in the filed application documents should be drawn up in compliance with relevant laws and regulations. These documents should include clear information and analysis of the financial conditions, business results and cash flow of applicant and its Affiliated companies; as well as details of related companies, research and development activities, major shareholders, officers and employees, dividend policies, planned use of funds raised by public offering, risk information and any other matters that may be valuable to investment decisions.

Information that should be included as risk factors :0 duration of business years, accumulated deficiency or operating loss, management dependency on certain members of the board, competitions in the industry, uncertainty of market and technology, management support from related party, items relating to prerequisite for principal business(Note), etc., which could be considered risky factors in investment decisions. (SRSLR: Art.7-(1)a(a))

(Note) Prerequisite principal business should include following items.

- (a) Prerequisite for the principal business of applicants
- (b)Duration of the prerequisite (if any such duration is provided by laws, regulations or agreements)
- (c)Events for termination or cancellation of the prerequisite (if any such event is provided by laws, regulations or agreements)
- (d) Whether any factor which will cause difficulties in maintenance of the prerequisite is likely to occur

(2) Accounting systems of applicant and its Affiliated companies should be appropriately prepared and managed according to the accounting principles employed. (SRSLR: Art.7-(1)a(b))

(3) Corporate disclosure of applicant and related companies should not be distorted as a result of transactions with person having special relationship (Note), related companies and other entities, or from adjustments to the ratio of stocks held in related companies. (SRSLR: Art.7-(1)a(c))

(Note) 'person having special relationship' means officers (directors including their stock purchase plan, an accounting counsellor (in case an audit corporation or a tax accountant corporation is appointed as the accounting counsellor, such member(s) of the corporation as officially assigned for the service), auditor(s), executive officers including any other senior members of an applicant with equivalent powers), their family members within second degree of consanguinity (henceforth "Officers") companies whose majority of voting right is owned by applicant's Officers, related companies, and their officers.

(4) Applicant should be able to handle and disclose any corporate information

appropriately and timely in accordance with their own rules and regulations.  
(SRSLR: Art.7-(1)a(d))

(5) Applicant should be able to disclose their business results appropriately and timely on quarterly basis. (SRSLR: Art.7-(1)a(e))

### [ Focus of Examination ]

Transparency is one of the key characteristics of Mothers, therefore disclosure is strongly emphasized. TSE's main concern will be whether the corporate information presented to public is accurate and straightforward for investment decision making.

First, TSE's examiners will try to understand the applicant's business, their industry, future plans, etc., through the documents submitted at application (company brochure, business plan, etc.).

Then, examiners will assess the accuracy of the corporate profile, risk factors and other information stated in Securities Report for Listing Application – Part I ('Part-I'). TSE may request applicant to add further information on particular data when necessary.

Examiners will see if the applicant's corporate system will be able to carry out timely disclosure at every quarter once it has been listed. Whether internal controls are properly managed according to applicant's size and industry will also be examined. Also, TSE may request an interview with the applicant's accounting counsellor, if the applicant has nominated one, in order to better understand how the company has built and maintained the internal structure and organisation responsible for accounting procedures as well as to check whether or not the applicant unduly relies handling of such accounting procedures on the accounting counsellor.

TSE will assess above elements by having interviews with applicant and their auditors by discussing how their accounting system is organized.

Information that should be included as risk factors in Part I are: duration of business years, accumulated deficiency or operating loss, management dependency on certain Officers, competitions in the industry, uncertainty of market and technology, management support from related party, prerequisite for principal business, etc., which could be considered risky factors in investment decisions. If

there is something as a prerequisite for principal business, such information should be stated as what it is, duration of the prerequisite if any such duration is provided by laws, regulations or agreements, events for termination or cancellation of the prerequisite if any such event is provided by laws, regulations or agreements, whether any factor which will cause difficulties in maintenance of the prerequisite is likely to occur. If there is any factor, such information is should be stated that the factor might affect applicant's business seriously.

TSE expects wide range of such risk factors, and applicant is required to openly disclose the information as much as they can. Therefore, although an applicant may find useful the following examples of risk factors, it is advisable to make every effort to disclose all other information necessary for correct and better understanding of its business as well as material facts, in a manner best suitable.

In addition, disclosure of company profile and business should be 'simple and straightforward' for making investment decisions, reflecting the applicant's true conditions.

#### **Risk Factors to be stated in the Securities Report for Listing Application – Part I (example)**

- **Applicant's business is still in its early stage and unsettled**
  - When it has been only a few years since applicant's corporate establishment, debt guarantee may be necessary.
  - Any factors that can obstruct applicant's business activities due to short duration of business years.
  
- **Applicant's countermeasures in the future business plan when it has no current profit recorded or has accumulated deficiency**
  - Profit may not be recorded due to initial expenses.
  - Applicant may have effective measures and policies for gaining profits.
  - There may be little possibility for recording profit for another few years. (the rule applies with consolidated subsidiaries as well)
  - When both amount and ratio of debts (includes contingent liabilities) are high, they may influence company's business result at the time of

increased interest rate.

- **Applicant's profit may be pressed by competitions, etc.**
  - Industrial environment and applicant's position, current and future competitors, their influence to applicant's profit, etc.
  
- **Business activities may be dependent on a particular party for management, technology knowledge, etc.**
  - Entrepreneurial companies often have fewer officers or employees and depend on a few particular people with particular skills. When such people leave the company, it may be difficult to replace them and thus, company business may be affected.
  
- **It takes time to commercialize newly developed products or technologies**
  - When extended period of time may be required for developing new products or new technologies, Research and Development expenses may be recorded during the period. Several years may be required before a new factory can function fully
  
- **The business depends on products and technologies whose possibilities are yet uncertain**
  - Although applicant's business has been operated by their own products and technologies, new comers may join the industry due to the lack of patent protection.
  - When applicant's products are in the market under license agreement with another company, future changes in the agreement may influence applicant's performance.
  - When applicant's business greatly depends on certain products, changes in industry or in contract terms with partners may affect applicant's performance.
  
- **Business may depend on partners/customers with unstable business continuity**

When applicant's purchases or sales depends on certain partners,

- it may become difficult to continue trading with them
- it may be difficult to replace them when services are terminated

○ **Business activities has to follow certain legal regulations or self-imposed restrictions**

- Applicant has been applied or to be applied by legal regulations
- Future changes in legislation may affect applicant's business

○ **Prerequisite for principal business**

- When there is prerequisite (i.e. permission, approval, license or registration required for the principal business or principal product; or distributorship agreement or manufacturing agreement relating to the principal business, or principal product) for principal business, applicant might be caused difficulties in its business and its business performance might be affected seriously, by termination or cancellation of the prerequisite.

○ **Applicant is involved with any serious lawsuits**

- Any law suits that might affect applicant's performance; patent property cases where a company with patent property may file a suit against applicant, which will affect applicant's business (patents on business models, etc.)
- No current cases, but legal cases may arise depending on future industrial circumstances

○ **Business industry may take drastic changes**

- When there is a possibility of sudden, drastic change in applicant's industry due to changes with new competitors, business environment, etc., they may affect applicant's business performance

○ **Transactions are made between applicant and person having special relationship**

- Applicant's Officers (and person having special relationship) have been

providing guaranty of liability and its amount or its time of dissolution may affect applicant business

○ **Major shareholders' involvements with applicant's corporate management**

- Major shareholders' involvement with company's management may affect company's business
- Company's business has been dependent on certain major shareholders and transaction termination with him/her may affect company's business performance

○ **Dilutions of shares, stock options exercise, etc.**

- Applicant has allotted stock options and exercising such options will reduce the value of each stock, unbalancing the short-term balance in stock market, and thus influencing stock price

○ **Future business plans**

- Plans to start new business
- Plans to expand current business
- There are is a possibility of business and legal risks related to above

○ **Policies on profits returns**

- Returning profits to shareholders is one of the critical responsibilities for any listed company. Company's policies on profit sharing, how to determine its dividend and details on internal reserves should be clearly stated.
- Even if there is no prospect for dividend in the immediate future, the policies should be clarified.

○ **Planned use of fund**

- The details of future usage of the fund assembled by coming IPO should be clearly stated.
- Investment risks (equipment fund, operating fund, settlements of debts, securities acquisition, investing and financing to related companies,

M&As, etc.) should be stated.

## **2 Sound Corporate Management (CLES: 5-1(2))**

TSE will examine whether applicant and its related companies are operating business fairly and faithfully (CLES: 5-1(2)).

Based on the belief that sound corporate management requires appropriate and adequate corporate governance, TSE will first look at an applicant's general ideas about corporate governance as well as how it addresses and implements its corporate governance policies.

Note: As one way to facilitate the above examination process, TSE will review "Corporate Governance Report" submitted by an applicant. For the details of the Report, please go to the following TSE website "Documents to Be Submitted by A New Listing Applicant."

[http://www.tse.or.jp/listing/b\\_listing/format/index.html](http://www.tse.or.jp/listing/b_listing/format/index.html)

The following is the specific criterion for examining the sound corporate management.

Applicant and its Affiliated companies are not making transactions with person having special relationship, HR/capital related companies or other entities, under conditions clearly disadvantageous to applicant. (SRSLR:7.b)

### **[ Focus of Examination ]**

Transactions between applicant and person having special relationship may have been conducted under condition that will bring particular interest to the special interest person. This, in turn, would be a disadvantageous deal for applicant, unfairly letting the benefit belong to person having special relationship instead of the duly authorized shareholders. This is against Mothers rule that a public company is responsible for appropriately sharing its profit with all its shareholders and this rule also applies with the rest of TSE's markets.

On the other hand, if applicant is having transactions under the condition that is favourable to applicant, with the view to support applicant by its Parent company, the contents of such transactions should be disclosed

Also, extra caution will be taken where officers and/or employers of the Parent company of an applicant has a minority stake in an applicant, or been allotted subscription warrants. This is because such an arrangement is not deemed legitimate or necessary either as means of ensuring management accountability or an incentive scheme unless officers and/or employers of the Parent company have direct involvement and responsibilities in the applicant's business operation.

### 3 Subsidiary Listing Rules

When applicant has its Parent company (Note)(except when it will not longer have one by the end of application year), following rules should be met along with the above 1 and 2.

(Note) 'Parent company' here means as stipulated in the Article 8-3 of Financial Statements Rules (*Zaimushohyou-tou Kisoku*) and a company whose 'affiliate company' is as stipulated in the Article 8-5 of Financial Statements Rules,

(a) There are not disadvantageous transactions imposed/induced between applicant (including its Affiliated companies) and its Parent company and vice versa. (SRSLR: 7.(1)c(a))

(b) The terms under which applicant (including Affiliated companies) and Parent company conduct business/transactions do not differ from the norm (i.e. in terms of prevailing market prices, etc.). (SRSLR: 7.(1)c(b))

(c) Applicant's Parent company should meet one of the criteria below. However, this does not apply when business relations between the parent and applicant companies are tenuous, and the stocks held by the Parent company are just for investment, and not for control purposes. (SRSLR: 7.(1)c(c))

- a. Parent company's shares are listed on a stock market in Japan or in foreign countries whose disclosure systems are fairly as same as one in Japan.

b. Parent company is a reporting company (a company which files corporate disclosure information with the authorities (and therefore available to the public) on a periodic basis), and the applicant has access to accurate information relating to the Parent company which will significantly affect management of the applicant. Furthermore, the Parent company has agreed in writing to the following conditions:

(a) The applicant shall submit copies of corporate disclosure information (e.g. annual, semi-annual and quarterly reports, etc.) filed with the authorities by the Parent company in its home country, to TSE for public inspection.

(b) The applicant shall file corporate disclosure information documents stipulated under Cabinet Office Regulations, Article 15-1-1(a) (hereafter 'designated corporate disclosure information documents') of its Parent company\* to TSE. This should be done annually for public access.

\* The filing would not be necessary if the Parent company has been filing its financial information to Financial Bureau of Japan.

(c) Applicant shall make prompt and appropriate disclosure of any corporate information about the Parent company which will significantly affect applicant's business operations.

### [ Focus of Examination ]

When applicant is a subsidiary of another company, in many cases, applicant is under the influence of Parent company. Parent company may support applicant by HR, funds, technology, transactions, etc. Therefore, TSE will see if applicant will be able to run its normal business without interference of Parent company, consequently, the interests of the stockholders will be protected.

There are times TSE inquires the purpose of its subsidiary's listing from Parent company.

As to subsidiary listing, TSE will examine following points.

(a) Applicant should be able to conduct its business activities and make business

judgment by itself, being not affected by its Parent company, even if it will be under the situation that there will be another company whose business will be similar to applicant in the same corporate group.

(b) There should be no disadvantageous transactions (business transaction, real-estate transaction, fund transaction, etc.) imposed/induced between applicant (including its Affiliated companies) and its Parent company and vice versa - If applicant is having transactions with its Parent company. These transactions should be caused by rational, necessary reason, and their condition should be appropriate.

(c) Directors of applicant should be able to make business decision by itself and for itself. Decision making of board should not be obstructed by the situation that no less than half of the members of the board, or of each management committee, are the Officers or employers of its Parent company, or that full time officers are on loan from its Parent company

(d) Applicant should not make its business decision by suggestion of its Parent company but by itself. Applicant business activity should be independent of its Parent company.

(e) Applicants should not be placed excessive constraint (agreement with its parent) on business activity by its Parent company.

(f) Securities Report for Listing Application Part1 should include clear information as to relation (contents of transaction, etc) between parent and applicant.

Parent company needs to, either; be a listed company, or file corporate disclosure information with the authorities on periodical basis. (hereafter 'public company') In a case where Parent company owns its subsidiary (applicant) just for investment purposes rather than to control them, above requirement will be exempted.

The contents of 'designated corporate disclosure information documents', which should be filed to TSE by Parent company and will be released for public, is as follows:

Type of Parent company	Corporate Disclosure Information
Corporations	<p>One of the following financial information should be filed to TSE:</p> <p>(a) Consolidated financial statements and Parent company's financial statements for the recent two years or</p> <p>(b) Consolidated account statements arranged under Companies Act, Article 444(4) and Parent company's account statements arranged under Companies Act <sup>(Note 1)</sup>, Article 435 for the recent two years</p> <p>(Note1) If applicant is the unique subsidiary, filing of consolidated account statements will be voluntary</p> <p>The above documents (a) and (b) need to have been audited by CPA in compliance with one of the following <sup>(Note 3)</sup>:</p> <p>(a) Securities and Exchange Law, Article 193-2 or</p> <p>(b) Companies Act, Article 328 and Article 444(4)</p> <p>(Note2) Audit reports could be reduced to the ones for the latest year (instead of recent two years) if Parent company's business is only to protect the assets of applicant's initial owners. If this case seems to apply, please contact TSE well in advance for TSE's assessment.</p>

<p>Government –affiliated corporations, etc.</p>	<p>In principal, same rules apply as in the cases where Parent company is a corporation. <sup>(Note 3)</sup></p> <p>(Note3) When the Parent company is keeping financial documents whose details overlap with ‘designated corporate disclosure information documents’, they can replace the designated documents with their own. However, they might be required to add information whenever the contents of the document is considered inadequate by TSE.</p> <p>Parent company needs to be audited under relevant laws such as each corporation’s establishment law and its audit report should be submitted to TSE.</p> <p>Even when the ownership of voting rights does not reach the majority, and thus the holding company is not legally defined as a ‘Parent company’, it may still be required by TSE to submit the ‘designated corporate disclosure information documents’ available for the investing public. This applies when the holding company has significant influence and control over the applicant.</p>
<p>Investment funds, etc.</p>	<p>In principal, same rules apply as in the cases where Parent company is a corporation. <sup>(Note 4)</sup></p> <p>(Note4) TSE may ask for further data other than those required in ‘designated corporate disclosure information documents’ when they deem useful for the investing public. If there is any difficulty disclosing certain information due to the fund’s current state, please contact TSE in advance.</p> <p>If the fund is practically controlled or significantly influenced by someone, the person will be deemed Parent company and be obliged to file the ‘designated corporate disclosure information documents’.</p> <p>Even when the ownership of voting rights does not reach the majority, and thus the investment fund is not legally defined as a ‘Parent company’, it may still be required by TSE to submit the ‘designated corporate disclosure information documents’ available for investing public. This applies when the investment fund has significant influence and control over the applicant.</p>

### **Frequently Asked Questions**

**Q :** Mothers' requirement is that applicant's Parent company (company that holds applicant's majority voting rights) is a public company (it's a listed company, or it files corporate disclosure information with the authorities on periodical basis). Are there any exceptions?

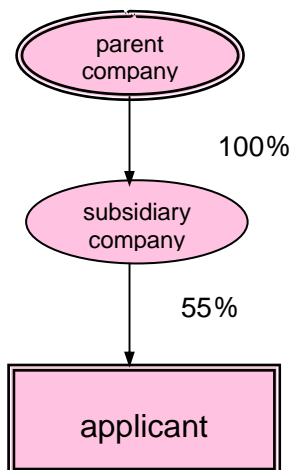
**A :** If the Parent company has been established for investment purposes and not to control or influence the business activities of the applicant, the applicant will be exempt from the requirement.

Example: A company that holds applicant's majority voting rights may be a venture capital and has no business transactions with applicant. This could be admitted an exception.

As for other cases, please consult TSE well in advance. Exception admission depends on individual circumstance.



Listing order: examples



Applicant's direct parent company, which owns 55% of applicant's shares, also has its 100% parent company. This means the applicant has two Parent company and the one which has more control and influence over the applicant needs to be a public company.

#### 4 Other Items in the Public Interest and for Investor Protection (CLES: 5-1(3))

(a) No factors that will cause difficulties in maintenance of 'prerequisite for principal business' exist.

#### [ Focus of Examination ]

'Prerequisite for principal business' here means permission, approval, license or

registration required for the principal business or principal product; or distributorship agreement or manufacturing agreement relating to the principal business or principal product.

If applicant requires permission, approval, license or registration to carry on its principal business, TSE will see whether the applicant will be able to renew the permission or others continuously.

If the prerequisite for principal business such as permission, approval, license or registration required for the applicant's business is cancelled, it might be impossible to maintain the principal business. Applicant's business might be affected if the distributorship agreement, or manufacturing agreement between subcontract factory and applicant like a fables company relating to the principal product is cancelled.

Therefore, TSE will see if there will be no factors that will cause difficulties in maintenance of prerequisite for principal business.

Additionally, applicant will be required to submit a document as to 'Prerequisite for principal business' including following items. And TSE examines this document.

Even if there is no 'prerequisite for principal business' for the applicant, applicant should submit the document that indicates so.

- (a) Prerequisite for the principal business of applicants
- (b) Duration of the prerequisite if any such duration is provided by laws, regulations or agreements
- (c) Events for termination or cancellation of the prerequisite if any such event is provided by laws, regulations or agreements
- (d) Whether any factor which will cause difficulties in maintenance of the prerequisite is likely to occur.

(b) No unfair restrictions on shareholders' right and exercise thereof.
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An applicant which adopts a takeover defence measures is advised to have sufficiently assessed legitimacy of such measures, especially in terms of its legal compatibility and what is acknowledged as "Corporate Value Standard", that is, the idea that introduction and exercise of any takeover defence measures should be

decided on the basis of whether a takeover proposal is likely to promote or damage a company's corporate value. In addition, takeover defence measures must not unfairly restrict shareholders' right or its exercise. Please note that an applicant is deemed unqualified for a listed company, should it adopt any of the following examples of takeover measures, all of which are understood to unduly restrict shareholders' right and its exercise.

#### Rights Issue without Piggy-Back Option

A type of takeover defence measures in which an applicant will allot share subscription rights to the shareholders at the time of introduction of such measures, at a significant discount to the market price of existing shares. (Excluding when such allotment is provisional, in that those found to be shareholders at the time of exercising the measures will be also allotted the equivalent rights.

Exercise of a takeover defence measures without piggy-back option is likely to cause a significant loss to the shareholders, whether or not they are a hostile acquire, who have bought the shares of an applicant after the day on which the rights are first allotted, due to dilution of value of the shares. Also pricing of the applicant's shares on the market will remain extremely volatile whenever the market perceives the applicant as possibly close to, but short of, exercising its defence measures. For the aforementioned reasons, takeover defence measures involving rights issues without piggy-back options unfairly restrict shareholders' rights and their exercise. Therefore, an applicant adopting this types of takeover defence measures are not eligible for listing.

On the other hand, a takeover defence measures involving what is often called entrusted rights issue, allows an applicant to have issued and entrusted share subscription rights to a trust and banking company, which will be allotted to the registered shareholders by the banking company in the event of a hostile takeover bid and its meeting the necessary conditions for invoking the defence measures. In other words the entrusted rights issue ensures that all shareholders, including those who have acquired the shares after the issuance and entrustment of the share subscription rights, are equally allotted the share subscription rights in the event of exercising the defence measures. Therefore, entrusted rights issue is considered to have piggy-back options, hence equivalent to other types of takeover defence

measures which do not require issuance of share subscription rights upon their introduction, such as contingency defence plans and others involving board resolutions setting conditions for invoking defence measures. Thus, an applicant will not necessarily be deemed disqualified for listing when its anti-takeover plan falls into this category.

#### Dead Hand Right Issue

A dead hand right issue which cannot be redeemed or prevented from invoking even when the majority of the board members at the time of when it was adopted are replaced by the shareholders' vote.

In the Takeover Defence Guidelines, published by the Corporate Value Study Group, a body set up by Ministry of Economy, Trade and Industry (METI), a dead hand right issue is condemned as contradicting "Corporate Value Standard" in that it blocks even those takeover bids which could possibly promote a company's corporate value.

At the same time, an applicant introducing takeover defence measures involving a dead hand right issue option effectively and unjustifiably prevents its shareholders from exercising the right to appoint as well as dismiss the management, through voting at a shareholders' meeting, thus failing to meet the above listing criterion. Therefore, we do not believe an applicant introducing a dead hand right issue is eligible for listing.

#### Issuance of Class Shares with Right to Refusal

An issuance, or resolution authorising thereof, of class shares with right to refusal, which requires an approval at a class-shareholders' meeting for appointment or dismissal of the majority of the board and any other matter of equivalent importance. (Except for when TSE deems that such an issuance, or resolution thereof, is unlikely to badly affect the shareholders' interests, considering an applicant's business goals, for what purposes and to what types of shareholders or investors it issues such class shares with right to refusal, and any other conditions attached.)

\* An applicant is also considered to have effectively issued class shares with right

to refusal, as described above, when:

- it is a holding company,
- one of its main subsidiaries issues class shares with right to refusal, or class shares with right to appoint directors, as defined in Companies Act Article 108(1) and in the Article 108(1) , respectively, to anyone other than the applicant, and
- TSE believes such issuance makes difficult successful completion of a takeover bid.

TSE believes that an applicant's shareholders are denied such important right as appointment or dismissal of directors, thereby failing to meet the above listing criteria, when the applicant has issued class shares which requires an approval at a class-shareholders' meeting for appointment or dismissal of the majority of the board. Therefore, an applicant adopting takeover defence plans involving such class shares is not considered to be eligible for listing.

Notwithstanding, TSE may approve of an issuance of class shares specified above, when it believes that the issuance is unlikely to damage the shareholders' and investors' benefit, when considering:

- the applicant's business purposes,
- the purpose of issuing class shares with right to refusal,
- types of shareholders and/or investors to which the applicant issues such class shares, and
- other rights and conditions attached to class shares.

A most likely circumstance in which the above conditions are met is, when an applicant is a privatised company with class shares with right to refusal issued to the government in order to prevent its business operations diverting from the national benefit for which the company was originally established.

As for when an applicant is a holding company, TSE may recognise that the shareholders' rights and exercise thereof are unduly restricted, if a subsidiary of the applicant issues class shares with right to refusal or with right to appoint directors.

(c) If an applicant adopts takeover defence measures, it must comply with the items specified in the Rules of Timely Disclosure Of Corporate Information By Issuer of

#### Listed Securities And the Like, 7(3)d(c))

If an applicant adopts takeover defence measures, it must pay due respect to all the four items below, specified in the Rules of Timely Disclosure Of Corporate Information By Issuer of Listed Securities And the Like, 7(3)d(c)).

The sufficient and necessary details of the takeover defence measures should be disclosed.

An applicant must disclose, in accordance with the Rules of Timely Disclosure Of Corporate Information By Issuer of Listed Securities And the Like, sufficient and necessary details of the takeover defence measures since such information serves as a basis on which shareholders decide whether to approve of such measures, or for investors decide whether to invest in the applicant.

The conditions for invoking takeover defence measures should be made clear and unequivocal.

The criterion aims at preventing an applicant from designing its takeover defence measures so as to allow the management to determine, in an arbitrary manner, the conditions for invoking or redeeming the takeover defence measures. The management might, where it is the main body to determine conditions for invoking or redeeming takeover defence measures, decide to do so in an arbitrary manner, thus lacking transparency in the decision making process. Not only does this fail to meet the "Corporate Value Standard", it also provides investors with limited information useful for making investment decisions, thus forcing them to trade in the applicant's shares unsure of its possible actions in response in the event of a hostile takeover bid.

The possible impact on the secondary market should be curtailed so as not to cause excessively instable price formation or contingent loss to investors.

An applicant must design its takeover defence measures so as not to allow extremely instable price formation or cause loss to values of shares held by the shareholders.

Due respect should be paid to the shareholders' rights and exercise thereof.

An applicant must pay due respect to the shareholders' rights and exercise thereof, in introducing any types of takeover defence measures, not necessarily specified above, but including other types such as those resulting in altering the voting rights of the shareholders, or cause loss to right to property.

<Other Consideration In Introducing Takeover Defence Measures>

(1) Disclosure

An applicant is required to disclose all the necessary details of its takeover defence measures in a news release as well as on its corporate website. In addition, the applicant must summarise the purposes and the scheme of its takeover defence measures in its Securities Report for Listing Application Part-1, and Corporate Governance Report together with the corporate website URL on which the details of the measures are available.

Specifically, the applicant must disclose the following in the news release and on its website.

- the purposes of introducing the takeover defence measures,
- the scheme of the takeover defence measures,
- the procedure to be followed in the event of a takeover attempt and,
- possible impact on the shareholders and the investors

\* The applicant must not fail to explain in detail, when disclosing the scheme of the takeover defence measures, the decision making body responsible for invoking and redemption of the measures as well as the conditions for such actions. Moreover, the applicant needs to explain comprehensively specific aspects which help make the plans more palatable and transparent to investors such as:

- requiring an approval at a shareholders' meeting for its introduction,
- setting an objective condition for redeeming the measures, such as requiring withdrawal of the measures when a bidder has bought, or attempts to buy, all the shares outstanding, or, the majority of shares with cash,
- setting an independent committee responsible for assessing a takeover bid where views of independent members weigh,

- seeking for advice from outside experts,
  - sun-set provision through which to review the defence scheme on a regular basis, such as at an annual shareholders' meeting, and/or,
  - necessary conditions for appointment and dismissal of directors as well as their term of office
- \* The applicant must make sure to include a word 'takeover defence measures' In the title of a news release related to its takeover defence measures,

## (2) Consideration Depending on Types of Takeover Defence Measures

An applicant is required to comply with the following guidelines in accordance with a type of takeover defence measures it adopts.

### Rights Issue

- Shareholders' Approval

It is crucial, in the light of due working of a takeover defence plan, that such a plan is so structured that shareholders' will, meaning general consensus normally expressed at a shareholders' meeting, not an opinion of individual shareholders, is to be appropriately and adequately considered in making decisions on whether to redeem or withdraw it.

Therefore, TSE will examine not only whether the plan is effectively a dead hand right issue, but also whether its structure makes difficult appointment or dismissal of majority of the board members at a single shareholders' meeting, by looking into voting requirements of shareholders' meetings regarding appointment and dismissal of directors, directors' term of office and so on.

- Decision Making Framework for Invoking the Measures

An applicant must ensure that decision making procedure as to invoking the takeover defence measures is transparent and not arbitrary largely influenced by the management.

In particular, investors need to know how an applicant tries to secure fairness and neutrality of decisions by the body actually responsible for deciding on whether or not to invoke a rights issue plan, including an independent committee that advises the board of directors on whether or not to accept a

takeover bid where the board is required to make decisions based on its advice. In this respect, TSE examines the following matters:

- whether it is possible for such decision making body to stay independent of the management of the applicant,

- whether the said decision making body is provided necessary level of expertise through, say, involvement of professionals in the related area, authority to conduct researches separately from the management and so on and/or,

- how such body is made liable for its decision, for example through composition of an independent committee, if any, between directors, auditors, and outside professionals

TSE also requires appropriate and adequate disclosure of aforementioned information.

However, when TSE decides the applicant does not provide a sufficient level of fairness and neutrality of the decision making body through such methods discussed above, it will check whether an applicant discloses explicit and objective conditions and standards for deciding whether or not to invoke a rights issue plan.

- Impact on the Secondary Market

Takeover defence measures, inevitably, lead to high level of fluctuations in the share price formation. In this regard, the applicant is reminded that it should try to minimise factors within the framework of its takeover defence measures possibly contributing to contingent loss for investors.

Specifically instability in the share price formation is possible when the applicant's rights issue plan allows the applicant to withdraw the decision to invoke it. On the other hand, it contributes to an increased corporate and shareholders' value, thus serves for an purpose of a takeover defence measures, that is, to provide for an equal negotiation platform with a possible bidder, that the plan enables the applicant to withdraw it once the bid is abandoned or the applicant reaches agreement with the bidder on the terms of the takeover over a higher bid price. Therefore, when an applicant's right issue plan is found to have the above mechanism, TSE requires the applicant to provide the related information sufficiently.

In addition, the Exchange will look into any other aspects of an applicant's right issue plan which could possibly lead to fluctuation in the share price formation.

#### Contingency Defence Plans in the Event of A Hostile Takeover Bid

Contingency defence plans are a type of takeover defence measures in which an applicant sets rules to be applied, in the event of a hostile takeover proposal, to a bidder as to disclosure of information about the bidder, the procedures to be followed and so on.

If an applicant's takeover defence measures fall into this category, it needs to make extra efforts to comprehensively disclose information related to the rules to be followed by a possible bidder in the event of a hostile takeover, thus providing a basis for shareholders and investors to decide on whether such rules are legitimate.

In particular, the applicant is expected to disclose the following details of its takeover defence measures:

- the body responsible for administering and applying the rules
- information to be disclosed by the bidder to an applicant and the procedure for disclosure and
- actions the applicant may take when the rules are followed/not followed by the bidder.

TSE requires the applicant to explicitly disclose the above information as well as explain whether its defence plans set the rules for treating a possible bidder with fairness. Specifically, the defence measures are considered to be fair if the rules:

- do not require a bidder to provide the applicant's shareholders and investors with more information than reasonably possible
- designate the reasonable, but not longer than unnecessary, period of time, in which the applicant evaluates the proposed takeover bid, and,
- do not allow the applicant to take excessive actions had the bidder failed to follow the rules.

If an applicant's takeover defence measures involving, where an bidder fails to follow the rules set as part of the measures, exercising what is in effectively a rights issue plan, the applicant needs to state it clearly in its disclosure material as well as to disclose information specified in the above .

### Issuance of Class Shares

An applicant must ensure that its issuance of class shares or share options does not possibly result in restricting shareholders' voting rights or infringing their right to property.

(For Reference: Definition of the Terms That Appear in This Section)

Terms	Definition
Takeover	Acquisition of a controlling stake in a company
Takeover defence measures/plans, anti-takeover measures/plans	Measures to be introduced, without the imminent presence of a hostile takeover bid, which give an applicant the right to issue shares or share options, not for the purpose of fund raising, but for preventing the bidder to from successfully completing its takeover proposal
Introduction (of a takeover defence measures)	Determining specific scheme of a takeover defence measures such as the right to issue new shares or share options
Invoke/Exercise/Trigger (a takeover defence measures)	Preventing hostile a takeover proposal from being successfully completed by putting into practice the specific scheme of a takeover defence measures
Redemption (of a takeover defence measures)	Doing away with a takeover defence measures already introduced, including buying back shares or share options issued as part of the measures' scheme
Rights issue/plan	A type of a takeover defence measures which gives an applicant the right to issue share options to existing shareholders except for a would-be acquirer.

Note 1: The above definitions are cited from "Ensuring and/or increasing corporate value and stakeholder profits: takeover defence guidelines" ("Takeover Defence Guidelines"), drawn up by METI and the Ministry of Justice.

Note 2: In the TSE Listing Rules and Regulations, takeover defence measures refer to those introduced without the imminent presence of a hostile takeover bid.

(d) Other matters that TSE deems necessary from the viewpoint of public interest or protection of investors.

For the investing public, applicant will be considered inappropriate to be a public company, if their business purposes and activities are illegal or offensive to public order and morals. TSE will assess the details of applicant from this point of view and others.

For example, while applicant's business purposes and profile are fine, they may be involved in legal cases or conflicts that would affect the applicant's business activities or performances. TSE will need to investigate such cases or performance as they may incur unexpected loss on investors.

If applicant is in its financial reconstruction state, examination will cover details of restriction of shareholders' rights, management system and its operation in order to confirm they are not questionable for investor protection.

If applicant, including its person having special relationship or main shareholders, has connection with gangs, gangsters, or any party that are deemed organized crime (hereafter 'gangs'), the applicant will be considered unsuitable for listing. This will include cases where; any member of applicant, its person having special relationship, its shareholders, or its business partners is a member of gangs; gangs are involved in applicant's corporate management; applicant, its person having special relationship, its shareholders, or its business partners are directly or indirectly involved in gangs by providing funds or other activities; applicant, its person having special relationship, its shareholders, or its business partners is having any kind of intentional association with gangs.

## **5 Interview Questions**

Now that profile of listing criteria and examination has been illustrated, the following is questions that will be asked by TSE's examiners at interviews with applicant.

Please note that they are only few and actual interview questions may differ depending on the size, industry and operation of each applicant's business.

### **(1) The Reason for Listing**

- (a) Please explain the specific reason (purposes, expected impact, etc.) your company is applying for listing

### **(2) Business Profile**

- (a) Please describe how your current business has been established (history, purposes, etc.) and how your business model has been constructed. Illustrate using presentation materials, brochures, actual products, etc.
- (b) If there are any significant contracts regarding business operation, please elaborate them.

### **(3) Business Plan, ROI Plan and Fund-raising Plan at Listing**

- (a) Please explain; (i) how to utilize the fund that is to be raised at listing, (ii) ROI plan for the investments made in (i). As for business plan, please illustrate in detail; company's management policy, conditions for drafting business plan, potential risks and its countermeasures, future plans for further development.
- (b) Please explain the company's financial outlook in the year of application. It is desirable to disclose financial outlook at the time of listing. If that is not feasible, please state the reasons as well as future policies for drafting and announcing financial outlook.
- (c) As for the utilization of the fund raised at listing, please give details (including the actual amount) of the following: fund for equipment/plant, fund for operation, fund for research and development, repayment of debt, acquisition of securities, investing/financing for the related companies.

(Note) In (a) above, 'conditions for drafting business plan' means necessary environment improvements in industry, company's strategies and countermeasures, etc. 'Future plans for further development' needs to be explained with estimated budget

and other premises.

#### **(4) Conditions of the Industry**

- (a) Please explain, if any, about regulations imposed on the industry, profile of government directive and the ministry in charge, size of the market (if possible to have the idea), recent developments in the market and its future outlook.
- (b) Please describe competitive position and how it can be maintained and strengthened.

#### **(5) Corporation Management and Internal Audit**

- (a) Please explain brief administration process of the products/services from purchase to sales.
- (b) Please explain the issues brought up by auditors/accountants and underwriter for the improvement of company's management system. Also state the company's countermeasures and strategies to them.
- (c) Please explain about internal audit: company's audit department, its staff, its tasks (coverage area, task items, etc.), procedure, recent implementation, etc. If there is no independent team for internal audit, please explain the alternative implementation.

#### **(6) Timely Disclosure**

- (a) Please explain about implementation of timely disclosure process including following points:
  - 1) The number of staff and its selection for the department of information disclosure, its future development once being listed.
  - 2) The internal system and the number of days to publish earnings brief note; annually (consolidated/single unit), semi-annually (consolidated/single unit) and quarterly (consolidated/single unit with audit report).
  - 3) Administration of confidential information (if applicant is partially

outsourcing its accounting operation, any measures employed to prevent information leakage)

- 4) Communication and cooperation system within group companies.
  - 5) Person in charge of confidential information and backup support during his/her absence.
- (b) Please explain about policies and ongoing efforts in terms of Investors Relations activities.
- (c) Please explain about the company's efforts and approaches to prevent insider trading.

### **(7) Parent company and Group Companies**

- (a) If you have Parent company, please explain about allocation of roles and responsibilities of each member company within the group controlled by Parent.
- (b) If you have commercial transactions with Parent and/or other members of its corporate group controlled by Parent, please describe the details (amount, terms, etc.).
- (c) If you are receiving support from Parent and/or other members of its corporate group controlled by Parent, please describe the details.

### **(8) Dealings with Officers and Major Shareholders**

- (a) Please describe how the current major shareholders came to be involved.
- (b) If you have commercial transactions with Officers or major shareholders, please describe the details (amount, terms, etc.).

### **(9) Conflicts, Legal Cases and Illegal Activities**

- (a) Please explain, if any, about ongoing or settled legal cases during the past three years and the application period. As for the cases with patent right or utility model, please refer to the opinions by your legal advisors (lawyers and patent attorneys).
- (b) Please explain, if any, about any illegal acts by your company and

corresponding fines, charges, guidance by authorities, during the past three years and the application period (for example, additional charge on corporate tax, violation of Antitrust Law). Also, please describe the company's action and effort to prevent such cases.

**( 10 ) Others**

- (a) Please explain the reason and background if your LU or auditor had been replaced in the past.
- (b) Please describe, if any, the details of shareholders agreement.
- (c) Please describe the company's efforts to avoid any contact with organized crime.

(Note) TSE does not impose any restriction on changing LU or audit corporation. However, TSE will need to check the background if there was a change after applicant's preparation for listing had started.