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**Delusions of Hostility:
The Marginal Role of Hostile Takeovers in Japanese
Corporate Governance Remains Unchanged**

Dan W. Puchniak *

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I. INTRODUCTION

Two decades ago, a love for hostile takeovers was largely limited to some American academics and highflying investment bankers on Wall Street who lived by the mantra "greed is good." Today, hostile takeovers are widely embraced by mainstream governments, academics, and corporate governance pundits around the world who assume that hostile takeovers are a prerequisite for an efficient system of corporate governance. This is a dubious assumption.¹

* This is an updated and condensed version of an article that was first published in the Berkeley Business Law Journal. I would like to thank the Berkeley Business Law Journal for their permission to reprint the article and excellent work editing the original published version. See, D.W. PUCHNIAK, *The Efficiency of Friendliness: Japanese Corporate Governance Succeeds Again without Hostile Takeovers*, in: Berkeley Business Law Journal 5 (2008) 195. I would like to thank Kyushu University and the Japanese Government for supporting the research for this article. Thanks also to John O. Haley, Kent Anderson, Leon Wolff, Luke Nottage, Tom Ginsburg, Kenichi Osugi, Mitsuhiro Kamiya, Michiaki Abe, Caslav Pejovic, Mark Fenwick and Hyeok Joon Rho for providing comments on earlier drafts. Special thanks to Harald Baum for excellent comments and editing. To my wife and best friend, Norah, thank you for being you.

Recent economic history suggests that hostile takeovers are anything but a prerequisite for an efficient system of corporate governance. Japan's miraculous rise from its postwar ruins to the world's second-largest economy was built on a system of corporate governance that thrived because of—not despite—the *absence* of hostile takeovers. This historical fact is well-known and widely accepted. Based on this alone, the assumption that hostile takeovers are a prerequisite for efficient corporate governance appears ahistorical and misguided.

However, with the burst of the bubble in the early 1990s and the “lost decade” of economic ruin that followed, the Japanese corporate governance model was widely viewed as a failed economic experiment. Its success without hostile takeovers was deemed irrelevant. Concurrently, in the 1990s, America's unprecedented accumulation of wealth propelled it to the position of the world's sole economic superpower. America's success was largely attributed to its unique market-based corporate governance model, which was purportedly driven by hostile takeovers. Global competition led governments around the world to “play catch-up” by developing their own hostile takeover regimes. The increasing prevalence of hostile takeovers throughout the developed world, especially in continental Europe, became “evidence” of their efficiency and necessity. The received wisdom became that countries either embrace a hostile takeovers regime (in some form) or accept suboptimal economic performance.

It is in this context that Japan's recent economic recovery from its now infamous “lost decade” provides a poignant counterexample. From 1997 to 2007, Japan transformed itself from being on the brink of one of the largest economic meltdowns in modern economic history to experiencing (from 2002 to 2007) its longest period of postwar economic expansion. This astounding recovery (hereinafter “the lost decade recovery”) was defined by massive reallocations of capital from inefficient firms and industries to more efficient ones. If one accepts that hostile takeovers are an essential mechanism for an efficient system of corporate governance—particularly in periods of restructuring—then one would expect that hostile takeovers played a major role in Japan's remarkable lost decade recovery.

This was not the case. In fact, the role of hostile takeovers was minimal. There was not a *single* successful hostile takeover of a major Japanese company during the lost decade recovery. Instead, true to its postwar tradition, corporate Japan successfully restructured through government intervention, bank-driven reallocation of capital, and orchestrated, friendly mergers—the antitheses of the American corporate governance model premised on hostile takeovers.

The conspicuous absence of hostile takeovers in Japan's lost decade recovery is even more remarkable considering that, in the opinion of most experts, market conditions for

1 For more detailed footnotes supporting statements made in the introduction, see D.W. PUCHNIAK, *The Efficiency of Friendliness: Japanese Corporate Governance Succeeds Again without Hostile Takeovers*, in: *Berkeley Business Law Journal* 5 (2008) 195, 197-204.

hostile takeovers during the lost decade recovery were close to optimal. Prior to and during the recovery, the bust-up values of a substantial percentage of Japan's listed companies were considerably more than their cumulative stock price. Stable shareholdings between firms, which were widely viewed as the most significant barrier to hostile takeovers in Japan, had substantially declined to levels that many claimed made them increasingly irrelevant. Shareholder activism, spurred on by charismatic cultural icons and buttressed by a substantial increase in foreign shareholders, led many to suggest that Japan's purported cultural aversion to hostile takeovers was no longer a major hindrance. Reforms to Japan's corporate law regime essentially made Delaware takeover jurisprudence part of Japan's legal framework. Indeed, many corporate governance experts considered Japan to be a utopia for hostile takeovers. Yet despite the pro-hostile takeover environment that emerged, there was not a single successful hostile takeover bid either prior to or during Japan's lost decade recovery.

Ironically, not only were successful hostile takeovers absent during the lost decade recovery, but the recovery appears to have reinforced the traditional Japanese corporate governance model (in which hostile takeovers play absolutely no role). Despite the poison pill being made legally available, banks and companies opted to substantially rebuild their cross-shareholdings. Shareholder activism was quelled by the prosecution and demise of Horie and Murakami—the two *de facto* leaders of the shareholder activism movement. The ostensibly “more efficient” US-style board structure, with its mandatory “independent” directors, was adopted by less than three percent of Japan's listed companies. These facts clearly demonstrate that the lost decade recovery inspired a movement *away* from, not towards, the American governance model based on hostile takeovers.

The conclusion that hostile takeovers played a minimal role in Japan's lost decade recovery will likely surprise both casual observers and Japan experts. This is because for two decades, a hopeful cadre of journalists, academics, lawyers, and M&A consultants has produced a veritable library of literature explaining why Japan has been on the brink of a vigorous hostile takeovers market similar to that in the United States. Recently, a number of luminaries in the field have even drawn strained comparisons between the *de minimis* effect that repeated *failed* attempted hostile takeovers had during Japan's lost decade recovery with the dramatic effect that the vigorous hostile takeovers market had on restructuring corporate America in the late 1980s. The myopic focus on predicting the arrival of hostile takeovers in Japan and straining to find comparisons with the evolution of American corporate governance has distorted the literature by creating the false impression that hostile takeovers have become an important mechanism in Japanese corporate governance. They have not.

This article aims to correct this distortion. It exposes, with the aid of case studies and empirical evidence, the fundamental flaws in claims by numerous Japan experts that hostile takeovers played a significant role in the lost decade recovery. The conclusion reached is that there is no credible evidence that hostile takeovers played anything more

than a *de minimis* role in the recovery. This should not surprise. Hostile takeovers have consistently played only a marginal role in postwar Japanese corporate governance.

Admittedly, the goal of this article is humble. It is limited to disproving the evidence that hostile takeovers were a significant force in the lost decade recovery. This article does not attempt to provide a positive explanation for how Japanese corporate governance—in the absence of hostile takeovers—engineered the recovery (in another recently published article, I make this more ambitious positive argument).

Despite this article's humble goal, I believe it has substantial merit. Japan's economic prowess makes it one of a select group of countries that is viewed by comparative corporate law and governance scholars as a potential model for improving corporate governance around the world. Particularly since the emergence of the current global financial crisis, Japan's lost decade and recovery have taken on a heightened importance as prominent policymakers have dissected this period in Japan's economic history for clues of how to deal with the financial crisis. Thus, a fundamental misunderstanding of the role that hostile takeovers played in the lost decade recovery may negatively impact on critically important corporate governance reforms that are now being undertaken around the world to remedy the defects that may have instigated the financial crisis.

The balance of this article will proceed as follows. Section two explains why the absence of *successful* hostile takeovers in Japan logically undermines any claim that hostile takeovers had an *ex post* effect on corporate governance during the lost decade recovery. Section three outlines Japan's long history of *failed* hostile takeovers to debunk the argument that the "novelty" of hostile takeover *attempts* during the lost decade increased their *ex ante* threat. Section four demonstrates that the marginal nature of hostile takeovers remained unchanged during the lost decade recovery. Section five explains the fundamental flaw in attempts to equate the substantial increase in takeover *bids* during the lost decade with an increase in the *ex ante* threat of hostile takeovers. Section six empirically demonstrates that during the recent recovery Japanese managers failed to embrace new legally available defensive measures to protect themselves from the purported threat of hostile takeovers—buttressing the conclusion that there was no significant threat at all. Lastly, section seven explains how Japan's "barriers" to hostile takeovers began to rebuild during the lost decade recovery—suggesting that hostile takeovers will remain a marginal force in Japanese corporate governance in the foreseeable future.

II. THE IMPACT OF *FAILED* HOSTILE TAKEOVERS IS LIMITED TO INCREASING *EX ANTE* THREAT

The absence of successful hostile takeovers during the lost decade recovery is a historical fact.² This fact presents a problem for the cadre of corporate governance experts who are intent on drawing strained comparisons between Japan's non-existent hostile takeovers market during the lost decade recovery and the vigorous hostile takeovers market that drove restructuring in the United States during the 1980s.³ As a result, some experts have tried to rely on failed hostile takeover attempts as evidence that hostile takeovers played a significant role in Japan's lost decade recovery.⁴ This argument is seriously flawed.

From a corporate governance perspective, hostile takeovers are important because, given that share price reflects expected company performance, outsiders who believe that they can improve a company's performance have an incentive to acquire its shares. In theory, competition among outsiders ensures that the company's resources will be acquired by the outsider who can run the company most efficiently. Efficiency is increased *ex post* as the acquirer replaces management who is either less competent or not acting in the best interest of shareholders. In this way, hostile takeovers ensure that managers and companies that do not maximize shareholder value do not survive. In addition, hostile takeovers raise efficiency *ex ante* because the threat of hostile takeovers forces incumbent management to maximize shareholder value and reduce agency costs.⁵

2 *Ibid.* 200.

3 C.J. MILHAUPT, *In the Shadow of Delaware? The Rise of Hostile Takeovers in Japan*, in: *Columbia Law Review* 105 (2005) 2171, 2176, 2189. For a synopsis of Milhaupt's article see, C.J. MILHAUPT, *In the Shadow of Delaware? The Rise of Hostile Takeovers in Japan* (synopsis), in: *Journal of Japanese Law* 21 (2006) 199. See also, C.T. HINES ET AL., *Doing Deals In Japan: An Analysis of Recent Trends and Developments For The U.S. Practitioner*, in: 2006 *Columbia Business Law Review* (2006), 355, 360; J.B. JACOBS, *Implementing Japan's New Anti-Takeover Defense Guidelines: Part I: Some Lessons from Delaware's Experience in Crafting "Fair" Takeover Rules*, in: 2 *New York University Journal of Law & Business* 2 (2006) 323, 327.

4 According to Schaeede, "whether or not a hostile bid is launched or eventually successful is not as relevant as the potential threat of a hostile takeover introducing managerial discipline." U. SCHAEDE, *Competition for Corporate Control: Institutional Investors, Investment Funds, and Hostile Takeover in Japan*, in: *Center on Japanese Economy and Business, Working Paper Series 4* (Columbia University 2006) 25-26, <http://app.cul.columbia.edu:8080/ac/bitstream/10022/AC:P:258/1/fulltext.pdf>;

MILHAUPT, *supra* note 3, 2183; see also R.J. GILSON, *The Missing Infrastructure*, in: 2004 *Columbia Business Law Review* (2004), 29; D.G. GRUENER, *Note, Chilled To The Pill: The Japanese Judiciary's Cool Reception Of The Poison Pill And Potential Repercussions*, in: *University of Pittsburgh Law Review* 67 (2006) 871, 895; C. CARYL, *End of a Rebel Culture?* in: *Newsweek International*, 30 January, 2006; M. NAKAMOTO, *A Takeover Battle Launched by the Upstart Livedoor is a Test of How Much Big Corporate Groups Can Protect Themselves Against Unwanted Attention*, in: *Financial Times*, 22 March, 2005.

5 M. BURKART / F. PANUNZI, *Takeover*, in: *European Corporate Governance Institute, Finance Working Paper No. 118* (2006) 3, http://ssrn.com/abstract_id=884080.

The *ex post* efficiency gains achieved by replacing underperforming management obviously do not arise in the case of failed hostile takeovers because incumbent management maintains their position *ex post*. In turn, the claim that failed hostile takeovers impact corporate governance is largely based on the assumption that they raise efficiency *ex ante* by increasing the perceived threat of successful hostile takeovers. Therefore, those who claim that failed hostile takeovers in Japan have significantly affected corporate governance are more accurately claiming that failed hostile takeovers have significantly increased the *ex ante threat* of successful hostile takeovers. As explained below, case study and empirical evidence do not support this conclusion.

III. FAILED HOSTILE TAKEOVERS DID NOT INCREASE EX ANTE THREAT BECAUSE THEY WERE NOT A NOVEL FEATURE OF THE LOST DECADE RECOVERY

In order to argue that failed hostile takeovers increased efficiency *ex ante* during the lost decade recovery, hopeful M&A pundits have erroneously claimed that hostile takeover attempts were a novel feature of the recovery. Labeling hostile takeover attempts as novel allowed experts to suggest that, even though all of the takeover attempts during the lost decade recovery failed, the novelty of the attempts increased the perceived threat of hostile takeovers and thus increased the *ex ante* efficiency of hostile takeovers in Japan.

A leading article by Milhaupt, which is based on a number of failed (but no successful) hostile takeover attempts between 2000 and 2005, illustrates how experts have exaggerated the novelty and significance of failed hostile takeovers during the lost decade recovery.⁶ Milhaupt admits that there were not any successful hostile takeovers during the recovery.⁷ However, he then erroneously declares that, “the unthinkable has happened”, “hostile takeovers have arrived in Japan”.⁸ Such a claim suggests that the mere presence of hostile takeover attempts during the lost decade recovery represented a dramatic shift in Japanese corporate governance. This is an error.

That hostile takeovers were attempted during the lost decade recovery is far from “unthinkable”. To the contrary, for decades the control rights of asset-rich Japanese companies with languishing stock prices have been sporadically targeted by maverick Japanese and foreign investors.⁹ Target companies in Japan have consistently used defensive measures, which have normally involved relying on assistance from friendly

6 See MILHAUPT, *supra* note 3, 2177-2181.

7 See *ibid.* 2181, 2184.

8 *Ibid.* 2171-2172.

9 M. TOKUMOTO, The Role of the Japanese Courts in Hostile Takeovers, in: *Law in Japan* 27 (2001) 1, 3-5.

stable shareholders, to prevent acquirers from successfully gaining control.¹⁰ On numerous occasions over the past several decades, acquirers have responded to these defensive measures by commencing legal proceedings in which they attempted to have the court set aside defensive measures on the basis that their “primary purpose” was to entrench target management and not to increase shareholder value.¹¹ In some instances, acquirers have succeeded in having Japanese courts strike down defensive measures.¹² In other instances (more often in the 1980s than during the lost decade recovery), aggressive shareholders have pressured target management to repurchase shares at a significant premium to avoid being acquired and to maintain their ultimate control.¹³ These facts about Japan’s hostile takeover environment over the last several decades are unremarkable when compared to the United States and to many other developed countries.

However, what distinguishes Japan from the United States, and most other developed countries, is that attempted hostile takeovers have been almost universally unsuccessful in removing control from target management.¹⁴ This did not change during the lost decade recovery. In addition, the trend that hostile takeovers have been attempted mainly by those outside of Japan’s established business community remained largely intact. Both the consistent failure of hostile takeovers to remove *de facto* control rights from Japanese management and their status as being driven mainly by marginal players in the business community have relegated hostile takeovers to a footnote in postwar Japanese corporate governance—even during the lost decade recovery.

An examination of the failed hostile takeover attempts in Japan prior to the burst of the bubble (which occurred in 1989–1990) demonstrates that failed hostile takeovers existed long before the lost decade recovery. Two of the most notorious large-scale hostile takeover attempts in the 1980s were Video Seller’s attempt to take over Fujiya and Trafalgar-Glen’s attempt to take over Minebea Company.¹⁵ While the Video Seller’s takeover attempt was driven by aggressive Japanese private investors and Trafalgar-Glen’s attempt by aggressive foreign investors, they shared a number of characteristics that are typical of failed hostile takeovers in Japan: (1) the hostile takeover targets were both large, well-established Japanese companies listed on the Tokyo Stock Exchange (TSE) (2) both targets had high asset values and languishing stock prices; (3) the

10 W.C. KESTER, *Japanese Takeovers: The Global Contest for Corporate Control* (Harvard Business School Press, 1990) 256; TOKUMOTO, *supra* note 9, 5-11; M. KAMIYA, *The Possible Implications of Japanese Court Decisions on Defensive Measures for Japanese Corporate Governance*, presented at Kyushu University’s Corporate Governance in East Asia Conference, 10 February, 2007 (unpublished paper, on file with author), 5.

11 S. MARTIN, *The Ultimate Barrier Revisited: Mergers and Acquisitions in Japan*, in: Oda (ed.), *Japanese Commercial Law. In an Era of Internationalization* (London, Kluwer Academic, 1994) 55; TOKUMOTO, *supra* note 9, 5-11.

12 See, e.g., *Shuwa v. Inageya*, Tokyo District Court, 2 July 1989, Hanrei Jihô 1317, 28.

13 KESTER, *supra* note 10, 237-262.

14 PUCHNIAK, *supra* note 1, 232.

15 KESTER, *supra* note 10, 239-244, 254-58.

acquirers were not part of Japan's business establishment; (4) the management of the target companies relied on friendly stable shareholders and other defensive tactics to dilute the acquirer's stake; and (5) management was ultimately successful in maintaining control.¹⁶

The Video Seller and Trafalgar-Glen cases reflect a wider trend of pre-bubble hostile share acquisitions in which management was able to maintain a firm grip on ultimate control. Every year from the late 1970s until the burst of the bubble in the late 1980s, there were several major share acquisitions of large listed Japanese companies by maverick Japanese investors with hostile intents.¹⁷ Although virtually every hostile share acquisition failed to remove control from management, many ended "successfully" for the acquirers as they "greenmailed" management of the target companies into repurchasing the shares they acquired at a premium in order to maintain their control.¹⁸ This trend was particularly pervasive from 1984 to 1988, during which Japan witnessed a rash of 23 successful greenmail transactions.¹⁹ None of these transactions removed ultimate control from entrenched managers, indicating that although these greenmail attempts "succeeded," the threat they ultimately posed to the control rights of Japanese management was marginal.

Koshin's acquisition of Kokusai Kogyo in December 1988 is the only case during the entire pre-bubble era in which a hostile acquirer successfully (albeit temporarily) removed ultimate control from incumbent management.²⁰ However, upon closer examination, even this supposed hostile takeover is evidence of the inability of hostile acquirers to remove successfully ultimate control from incumbent Japanese management.²¹

Early in 1989, immediately following Koshin's supposedly "successful" hostile takeover, the transaction was mired in criminal allegations related to Koshin's on-market acquisition of the target's shares. The allegations led Japanese regulators to indict numerous parties involved in the takeover on charges of insider trading, stock price manipulation, violations of banking regulations, and tax fraud.²² Under the pressure of

16 *Ibid.*

17 *Ibid.* 247-248.

18 *Ibid.* 237-262.

19 *Ibid.* 247-248.

20 In December 1988, Koshin exercised its rights as a holder of over three percent of Kokusai Kogyo's shares and requisitioned an extraordinary general meeting. In the meeting, Koshin used its majority stake to elect 15 new outside directors. This gave Koshin a majority of the directors on the board and ultimate control of Kokusai Kogyo. JOE J. LUFKIN, Flash in the Pan, in: IR Magazine 2000, http://www.thecrossbordergroup.com/ir_archive/pages/798/June+2000.stm?article_id=9435; J. STERNGOLD, Light Penalty for Speculator in Japan Stock Manipulation, in: New York Times, 20 May, 1993.

21 Arguably, this makes Koshin's acquisition of Kokusai Kogyo the only successful hostile takeover of a major corporation in postwar Japan.

22 Perhaps, the most disturbing allegation was that four of Kokusai Kogyo's senior executives had inside information about Koshin's plan to attempt a hostile takeover and then purchased

this enormous scandal, within a few months of this “successful” hostile takeover, Koshin lost control of Kokusai Kogyo’s board.²³ A little over a year later, Mitsuhiro Kotani, the infamous greenmailer who led Koshin’s hostile takeover, was pressured to resign as Chairman of Kokusai’s board and was later convicted of tax evasion charges in a related transaction.²⁴

Rather than serve as a threatening precedent to Japan’s entrenched incumbent management, Koshin’s disastrous and temporary takeover of Kokusai Kogyo did the opposite. It reinforced the image of hostile takeovers in the pre-bubble era as marginal players in corporate governance that were doomed to ultimate failure. During the lost decade recovery, this historical trend of failed hostile takeovers—which presented a marginal threat to the control of entrenched corporate management—continued.

In addition, as was the case during the lost decade recovery, prior to the burst of the bubble, Japanese courts played a significant role in regulating hostile takeover attempts.²⁵ In the late 1980s, it was common for companies to issue shares to friendly shareholders as a defensive measure to dilute the hostile acquirer’s stake.²⁶ In several of these cases, hostile acquirers responded to these defensive measures by commencing injunctive proceedings, under Article 280-10 of the *Commercial Code*, to suspend the issuance of shares by the target company.²⁷

shares based on that information, which they later sold at a profit when Koshin began secretly acquiring shares on the open market. J. STERNGOLD, *Four Arrested in Japan in Stock-Trade Scandal*, in: *New York Times*, 20 May, 1993; S. WAGSTYL, *Insider Trading Suspected in Japan’s Latest Share Scandal*, in: *Financial Times*, 15 June, 1990; see generally “Fugitive Businessman Arrested in Sydney”, *Daily Yomiuri*, 17 October, 1990; “Kotani Associate Hid 1 Billion Yen”, *Daily Yomiuri*, 12 April, 1991; “Stock Speculator Gets Prison Sentence for Tax Evasion”, *Japan Economic Newswire*, 27 April, 1992; “Sumitomo Executives Resign Amid Loan Scandal”, *United Press International*, 16 October, 1990; “10-YR Imprisonment Demanded for Janome Extorter”, *Jiji Press Ticker*, 20 December, 1999.

23 On February 23, 1989, ten members resigned from Kokusai Kogyo’s board. Seven of the directors that resigned had been placed on the board by Koshin in the December 1988 extraordinary shareholders’ meeting in which Koshin removed ultimate control from incumbent management by electing a majority of directors to the board. Following the resignation of Koshin’s seven directors, Kokusai Kogyo’s board was composed of 11 original members (i.e., those on the board prior to the takeover) and eight members placed on the board by Koshin. Thus, incumbent management had regained substantial control of Kokusai Kogyo. “10 Resign From Kokusai Kogyo Board”, *Jiji Press Ticker*, 23 February, 1989.

24 KESTER, *supra* note 10, 17; “Corporate Raider Given Suspended Sentence”, *Asahi News Server*, 19 May, 1993.

25 In his article in 2000, Minoru Tokumoto, discusses four cases in the late 1980s in which the court issued judgments in response to proceedings commenced in reaction to defensive measures implemented by a target company in the context of a hostile takeover attempt. TOKUMOTO, *supra* note 9.

26 See *e.g.*, KESTER, *supra* note 10, 256; KAMIYA, *supra* note 10, 5; TOKUMOTO, *supra* note 9, 5-11.

27 See TOKUMOTO, *supra* note 9, 5-11; see also MARTIN, *supra* note 11, 55.

In the late 1980s, as a result of a number of cases being brought before the court, a judicial test was developed for determining the circumstances under which target management could issue shares to friendly shareholders. According to this test, if the primary purpose of the issuance were to raise capital for the target company then the court would not suspend the issuance.²⁸ The jurisprudence surrounding this test, which came to be known as the “primary purpose test”, illustrates that the involvement of Japanese courts in hostile takeover battles was also not a novel feature of the recent recovery.²⁹

Failed hostile takeover attempts, and the court’s role in policing them, did not end with the burst of the bubble. In November 1989, just as the bubble was about to burst, T. Boone Pickens, a Texas billionaire and infamous American corporate raider, commenced a high profile hostile takeover attempt against Koito Manufacturing, a parts supplier and member of the Toyota *keiretsu*.³⁰ The Pickens-Koito takeover battle began when Pickens, who was widely criticized by the Japanese business establishment, secretly acquired a twenty percent stake in Koito from a well-known Japanese green-mailer.³¹

This sparked a two-year takeover battle that included an unsuccessful court action by Pickens to use his shareholdings to gain information about Koito’s finances, complaints by Pickens to the United States Congress that Koito’s stable shareholding relationships amounted to unfair trade practices and the refusal by Koito to allow Pickens any representation on the board.³² In 1991, Pickens finally admitted that he could not defeat Koito with its stable Toyota *keiretsu* shareholders and sold the shares he had acquired without a profit.³³ As expected, Koito’s management remained firmly entrenched.

In 1996, Japan experienced another high profile hostile takeover attempt when Masayoshi Son, of Softbank and Yahoo! fame, joined forces with Rupert Murdoch, the Australian media baron and takeover mogul, to acquire TV Asahi, one of Japan’s five main private broadcasters.³⁴ Similar to T. Boone Pickens’ attempt, the hostile takeover attempt by Son and Murdoch was “widely abhorred by the [Japanese business] estab-

28 TOKUMOTO, *supra* note 9, 4.

29 See Corporate Value Study Group, METI-Sponsored Corporate Value Report 2005, 13: available at http://www.meti.go.jp/policy/economic_organiza-tion/pdf/houkokusyo_hontai_eng.pdf. For a summary of the Corporate Value Report 2005, see Corporate Study Group, Corporate Value Report 2005 (Abstract), in: *Journal of Japanese Law* 21 (2006) 137. For a concise explanation of how the corporate value report relates to Japan’s new regime for regulating hostile takeovers see, H. BAUM, Takeover Defenses in Japan: Corporate Value Reports and Guidelines, in: *Journal of Japanese Law* 21 (2006) 131.

30 P.C. REICH, T. Boone Pickens and Corporate Governance in Japan: A Retrospective View of Three Sides of the Story and Recent Developments, in: *Law in Japan* 27 (2001) 27.

31 *Ibid.* 29.

32 See *ibid.* 29-36.

33 See D. IBISON, Prospect of Takeovers Becomes Hot Topic, in: *Financial Times*, 30 March, 2005; REICH, *supra* note 30, 31-33.

34 “Media Mould-Breakers”, Campaign, 24 March, 2006.

ishment".³⁵ After Son and Murdoch managed to acquire a twenty-one percent stake in TV Asahi, the entire Asahi media group rallied around TV Asahi.³⁶ Three months later, Son and Murdoch "cried uncle," selling their TV Asahi shares to Asahi Daily Shimbun (the group's daily newspaper) at no profit.³⁷ The control of TV Asahi's management was never seriously threatened by the failed hostile takeover attempt.

The pervasiveness of failed hostile takeover attempts prior to the burst of the bubble and during the lost decade demonstrates that they were not a novel feature of the lost decade recovery. The court's involvement in regulating Japan's lackluster hostile takeover regime is also not new to the recovery. Indeed, even claims by experts that failed hostile takeover attempts represent a revolution in Japanese corporate governance are not novel.

In 1991, Carl Kester, in his leading book on Japanese takeovers, claimed that failed hostile takeovers suggested a dramatic shift in Japanese corporate governance towards the American hostile takeovers-based model.³⁸ Kester also predicted, based on the failed hostile takeover attempts of the 1970s and 1980s (particularly, Video Seller and Trafalgar-Glen), that Japan would develop "a newly active market for corporate control" that would "no doubt" feature a "few surprising and notable successful hostile takeovers".³⁹ As two decades have passed since Kester published his book and there have been no "surprising [or] notable successful hostile takeovers", his predictions are obviously incorrect. The inaccuracy of Kester's predictions further casts doubt on similar, more recent, predictions by experts that "novel" hostile takeover attempts during the lost decade recovery represent a dramatic shift towards the American governance model.

In sum, the history of failed hostile takeovers by maverick investors prior to the lost decade recovery is important because it illustrates that the hostile takeover attempts that occurred during the lost decade recovery were not novel. Aggressive investors attempting to exploit asset rich companies with floundering stock prices have long been a part of Japanese corporate governance. The use of defensive measures and court actions in the context of these hostile takeover battles is also nothing new. Even claims by experts that rely on failed hostile takeover attempts as evidence of the arrival of an American-style market for corporate control have a long history. Far from being "unthinkable," the failed hostile takeover attempts during the lost decade recovery and the familiar predictions by experts that these mere attempts suggest a dramatic shift in Japanese corporate governance were completely predictable.

35 *Ibid.*

36 *Ibid.*

37 NAKAMOTO, *supra* note 4.

38 KESTER, *supra* note 10, 239.

39 *Ibid.* 18 and 239.

IV. THE CONTINUED HISTORY OF FAILED HOSTILE TAKEOVERS DURING THE LOST DECADE RECOVERY RECONFIRMED THEIR MARGINAL ROLE IN JAPANESE CORPORATE GOVERNANCE

The continued history of failed hostile takeovers during the lost decade recovery created a serious problem for experts who were intent on demonstrating that Japan developed a hostile takeovers market reminiscent of the United States in the 1980s.⁴⁰ This led many experts to exaggerate the significance and pervasiveness of hostile takeovers during the lost decade recovery. In some cases, experts reported hostile takeovers when none existed.⁴¹ In other cases, overly exuberant pundits prematurely claimed that “Japan’s first successful hostile takeover was nearing completion,” only to see the hostile bid soundly defeated in traditional fashion.⁴² In yet other cases, a number of experts accurately acknowledged the persistent failure of hostile takeovers during the lost decade recovery, but then erroneously claimed that these failures were of “epoch-making significance”;⁴³ the “nail in the coffin for old Japan Inc.”;⁴⁴ and marked “the advent of an era of hostile takeovers [in Japan].”⁴⁵ As in the past, failed hostile takeovers merely reconfirmed that Japanese management, not shareholders, maintained a firm grip on corporate control—precisely the opposite of the dramatic shift in Japanese corporate governance that many experts claimed these failed hostile takeovers to represent.⁴⁶

Before examining the details of the most prominent failed hostile takeovers during the lost decade recovery, it is necessary to re-examine transactions that have been held out to be hostile takeovers, which upon closer inspection, were not. A number of experts who credit hostile takeovers with transforming Japanese corporate governance during the lost decade recovery cite the 1999 acquisition by Cable & Wireless (“C&W”) of International Digital Communications (“IDC”) and the 2000 acquisition by Boehringer

40 See *supra* note 2.

41 See U. SCHAEDE, *The Strategic Logic of Japanese Keiretsu, Main Banks and Cross-Shareholdings, Revisited*; Center on Japanese Economy and Business, Working Paper No. 247, 2006, 32, <http://app.cul.columbia.edu:8080/ac/bitstream/10022/AC:P:259/1/fulltext.pdf>; “A&O Must Make the Most of Its Long-Awaited Japanese Entry”, *Lawyer*, 19 March, 2007; N. MATSUKO, ‘Market for Corporate Control’ for Better Governance in Japan, in: Economic Conference and Symposium, *Corporate Governance in the New Japan*, 3 November, 2003, 4 (unpublished PowerPoint presentation, on file with author); HINES ET AL., *supra* note 3, 225; R. NEFF, *Japan: Land of the Hostile Takeover?*, in: *Business Week*, 13 March, 2000; H. MIYAJIMA / F. KUROKI, *The Unwinding of Cross-Shareholding in Japan*, in: Aoki et al. (ed.), *Corporate Governance in Japan* (Oxford University Press, 2007) 79, 119.

42 C. SMITH, *Will Livedoor Open the Door?*, in: *Deal*, 8 July, 2005.

43 “M&As shake Japan’s corporate mindset, give hope for future”, *Nikkei Weekly*, 11 December, 2006; see also, MILHAUPT, *supra* note 3, 2173-2174, 2216.

44 M. FACKLER, *Mergers and Acquisitions No Longer Shock Japanese*, in: *New York Times*, 29 March, 2007.

45 “Reality check for new-media mirage”, *Weekend Australian*, 21 January, 2006.

46 G. JACKSON / H. MIYAJIM, *Introduction*, in: Aoki et al. (eds.), *Corporate Governance in Japan* (Oxford University Press, 2007) 9.

Ingelheim (“B&I”) of SSP as the beginning of Japan’s “new era of hostile takeovers.”⁴⁷ Despite such claims, both of these transactions were friendly acquisitions that bared no resemblance to a hostile takeover.

One such example was C&W’s acquisition of IDC. Although dubbed as one of Japan’s first “successful hostile takeovers,” it was nothing of the sort.⁴⁸ In 1998, the early stages of the IDC transaction occurred when IDC, a Japanese international telecom company, tendered for advice on its upcoming sale.⁴⁹ Almost everyone in the market saw the tender as a mere formality because it was widely assumed that IDC was destined to be bought by NTT, Japan’s former state telephone monopoly.⁵⁰ However, in March 1999, C&W, a British international telecom company, which was already a large stable shareholder of IDC, made a surprising offer to purchase it.⁵¹ NTT quickly countered with an offer of its own.⁵²

IDC’s board held an extraordinary meeting to consider the two competing offers and expressed its general preference for the specific terms of the NTT offer.⁵³ Following IDC’s board meeting, C&W revised the terms of its offer and significantly increased the premium of its bid on two occasions in response to counter offers made by NTT.⁵⁴ IDC’s board remained neutral throughout the balance of the transaction and offered no further recommendations.⁵⁵ At no time did IDC’s management-controlled board attempt to use any takeover defenses or suggest which bid its shareholders should support based on C&W’s revised offers.⁵⁶ In fact, the only recommendations following C&W’s revised offers were from Toyota and Itochu, two of IDC’s major stable friendly shareholders, who publicly announced their decision to sell their 17.7 percent stake in IDC to C&W.⁵⁷ In the end, a resounding 134 of IDC’s 141 major stable shareholders chose to tender their shares to C&W.⁵⁸ C&W ultimately acquired control of IDC because its

47 See, e.g., GILSON, *supra* note 4, 23; HINES ET AL., *supra* note 3, footnote 225; MATSUKO, *supra* note 41; “Weapons Needed to Fight Takeovers”, *Nikkei Weekly*, 27 September, 2004.

48 HINES ET AL., *supra* note 3, footnote 225; JACKSON/MIYAJIMA, *supra* note 46, 15; MATSUKO, *supra* note 41; See, D.H. WHITTAKER/M. HAYAKAWA, *Contesting “Corporate Value Through Takeover Bids in Japan*, in: *Journal of Japanese Law* 23 (2007) 5, footnote 2. See also E. COLCERA, *The Market for Corporate Control in Japan* (Springer, New York, 2007), 60-62 and 109.

49 COLCERA, *supra* note 48; “Shareholder Power”, *Economist*, 27 November, 1999.

50 *Economist*, 27 November, 1999, *supra* note 49.

51 See *ibid.*; “IDC’s Board Votes in Favor of NTT’s Takeover Offer”, *Japan Times*, 15 April, 1999.

52 *Economist*, November 27 1999, *supra* note 49.

53 COLCERA, *supra* note 48, 110.

54 “C&W Makes New Takeover Bid for IDC”, *Japan Times*, 6 May, 1999; “C&W Secures 97.69% Stake in IDC”, *Japan Times*, 16 June, 1999.

55 COLCERA, *supra* note 48, 109.

56 *Ibid.*

57 “C&W Wins IDC Stakes”, *Japan Times*, 9 June 1999.

58 *Japan Times*, 16 June, 1999, *supra* note 54.

revised offers were unopposed by IDC's management and supported by IDC's stable friendly shareholders—precisely the opposite of a hostile takeover.

Like the IDC transaction, the acquisition in 2000 of SSP, Japan's fourth-largest supplier of over-the-counter drugs, by B&I, a large German drug company, is also erroneously described as one of Japan's "first successful hostile takeovers."⁵⁹ Despite these claims, from the outset, B&I's acquisition lacked the hallmarks of a hostile takeover. B&I and SSP were long-time business partners, with SSP acting as the distributor for B&I's products in Japan.⁶⁰ B&I also had a seat on SSP's board and was a significant stable shareholder of SSP, with a 19.6 percent stake—hardly the profile of a corporate raider.⁶¹

In 2000, B&I made a successful unsolicited bid for a controlling stake in SSP, offering a forty-two percent premium to SSP's shareholders.⁶² There is no evidence that the bid was hostile in nature. To the contrary, B&I actively assured investors that the bid was not hostile and SSP's management remained neutral throughout the entire bid.⁶³ B&I's friendly relationship with SSP's incumbent management is evident from the fact that B&I chose to leave all of SSP's management in place after its acquisition was complete—something that does not always occur even in friendly takeovers.⁶⁴

Experts also refer to the 2004 Sumitomo Trust-UFJ dispute as evidence that Japan developed a hostile takeovers regime during the recent recovery.⁶⁵ Again, this claim is confused. The Sumitomo Trust-UFJ dispute did not even involve a hostile takeover *bid*, let alone a successful hostile takeover. The dispute, however, did involve an interesting contractual issue and competing merger bids between Japan's largest banks, but that misses the point. It is simply misleading to portray the Sumitomo Trust-UFJ dispute as an "epoch changing" transaction that marked a new era of hostile takeovers in Japan.⁶⁶

The facts in the Sumitomo Trust-UFJ case are straightforward. In May 2004, UFJ Holdings entered into a memorandum of agreement to sell its most profitable entity, UFJ Trust Bank, to Sumitomo Trust.⁶⁷ A term of the agreement was that Sumitomo Trust had the exclusive right to acquire UFJ Trust Bank during a two-year period and that neither party could engage in discussions with third parties that could have interfered

59 See MATSUKO, *supra* note 41; NEFF, *supra* note 41; see also "Ever So Polite", *Economist*, 17 February, 2001; CORPORATE VALUE REPORT 2005, *supra* note 29, 14. See also generally, WHITTAKER / HAYAKAWA, *supra* note 48, footnote 2.

60 COLCERA, *supra* note 48, 59.

61 J. CHOY, Win or Lose, More Players Join Japan's Mergers and Acquisitions Game, in: Japan Economic Institute (JEI Report No. 9 Mar. 3, 2000).

62 *Ibid*; SMITH, *supra* note 42.

63 SMITH, *supra* note 42.

64 *Ibid*.

65 MILHAUPT, *supra* note 3, 2177-2178.

66 See *ibid*. 2173-2174, 2177-2184.

67 See *ibid*. 2177-2178.

with the potential acquisition (“the no shop clause”).⁶⁸ In July 2004, UFJ appeared to violate this “no shop clause” by having discussions with Mitsubishi Tokyo Financial Group (MTFG) about a transaction in which MTFG would acquire all of UFJ’s business operations, including UFJ Trust Bank.⁶⁹

In response to the MTFG-UFJ discussions, Sumitomo Trust commenced legal proceedings to stop the MTFG-UFJ transaction on the basis that it breached the “no shop clause.”⁷⁰ After Sumitomo Trust’s legal action failed, it publicly threatened to launch a hostile bid for UFJ. However, in the end, Sumitomo’s threat of launching a hostile takeover bid was just a threat. In the fall of 2005, the MTFG-UFJ merger closed and Sumitomo Trust did not launch a hostile takeover bid.⁷¹ Characterizing the MTFG-UFJ transaction as evidence of Japan developing a U.S.-style hostile takeovers market is simply inaccurate.⁷²

If mis-describing friendly transactions or contractual disputes as hostile takeovers is confusing, then mistaking takeover *bids* with actual hostile takeovers compounds the problem. In a recent article, Ulrike Schaede, an Associate Professor of Japanese Business at the University of California, claims that “in 2005 a total of 53 successful hostile takeovers were recorded [in Japan]”.⁷³ In reality, there was not a single successful hostile takeover in Japan in 2005. It is likely, therefore, that Schaede has confused takeover *bids* (many of which were not hostile) with successful hostile takeovers.⁷⁴ As takeover bids in Japan do not even serve as a valid proxy for the *threat* of hostile takeovers (see next subsection below), these 53 cases do not lend support to her conclusion that hostile takeovers became a significant feature of Japanese corporate governance during the recent recovery.⁷⁵ In another article, *The Lawyer Magazine* reports that, in August 2006, Japan experienced its “first-ever hostile takeover” when Oji Paper acquired Hokuetsu Paper Mills.⁷⁶ As described in more detail below, Oji’s bid for Hokuetsu was defeated. The claim by *The Lawyer Magazine* is simply wrong.

Despite the exaggerations, mis-descriptions and false claims by experts, there were several failed hostile takeover attempts that actually did occur prior to and during the lost decade recovery. These failed hostile takeovers are noteworthy because they illustrate the ability of entrenched Japanese management to defeat consistently hostile take-

68 See *ibid.*

69 *Ibid.*

70 *Ibid.*

71 *Ibid.*

72 *Ibid.* 2182-2183.

73 SCHAEDE, *supra* note 41, 32.

74 The total number of takeover bids in Japan in 2005 was 53—which is the same as the purported number of “successful hostile takeovers” reported by Schaede. See RECOF’s webpage for a chart displaying the number of takeover bids in Japan from 1972 until present: <http://www.recof.co.jp>.

75 SCHAEDE, *supra* note 41, 32.

76 LAWYER, 19 March, 2007, *supra* note 41.

overs. In addition, they demonstrate that hostile takeovers are still largely launched by those outside of Japan's established business community and that relying on friendly stable shareholders is still a primary mechanism for incumbent management to defeat hostile attempts. In this sense, the failed hostile takeovers of the lost decade recovery are a continuation of the history of failed hostile takeovers in Japan over the past several decades.

In January 2000, Yoshiaki Murakami, a man described at the time as "a corporate raider" who preached "a very American sounding gospel of shareholders' rights and free markets," launched what many claim was Japan's first domestic hostile takeover bid.⁷⁷ Through his takeover boutique, M&A Consulting ("MAC"), Murakami targeted Shoei Corporation, a little-known electronics and real estate company that was part of the Fuyo (Fuji Bank) *keiretsu*. Shoei's cumulative stock price of \$66 million and \$570 million in liquid assets made it characteristic of a significant percentage of companies on the TSE that made Western pundits repeatedly predict that a wave of hostile takeovers in Japan was inevitable.⁷⁸

On January 24, 2000, MAC made a tender offer for all of Shoei's outstanding shares, with a forty percent premium over the 1999 market price.⁷⁹ Murakami's move made media headlines, but as an unwelcome outsider, he garnered little respect from Shoei's president, who refused to speak with him.⁸⁰ Despite the substantial premium offered, MAC's bid failed miserably, accumulating only 6.5 percent of Shoei's shares.⁸¹ The reason for the failure was predictable. In traditional fashion and unlike the American takeover market, stable and friendly shareholders gave unconditional support to existing management and refused to tender their shares to the "unwelcome bidder" regardless of the premium.⁸²

In December 2003, the next widely publicized hostile takeover attempt took place when Steel Partners, an aggressive American buyout fund, attempted to takeover Sotoh, a wool fabric company, and Yushiro Chemical Industry.⁸³ Both companies were extremely attractive takeover targets since their cumulative stock prices were lower than their liquidated asset values and they had significant cash holdings.⁸⁴ Steel Partners, which already had a ten percent stake in each of the companies, made takeover bids for each company with a thirty percent premium over their previous closing prices.⁸⁵

77 "Challenging Japan's Cozy Corporate Culture", *Time Asia*, 7 February, 2000.

78 *Ibid.*

79 COLCERA, *supra* note 48, 110.

80 *TIME ASIA*, 7 February, 2000.

81 COLCERA, *supra* note 48, 110.

82 P. LEE, A New Generation Embraces M&A, in: *Euromoney*, February 2006.

83 See MILHAUPT, *supra* note 3, 2180-2181.

84 See *Ibid.* 2180.

85 *Ibid.* 2180-2181.

In both cases, incumbent management “immediately announced their opposition to the unsolicited bids and, as a defensive measure,” substantially increased their dividends.⁸⁶ The substantial increase in dividends caused the share price of both companies to increase dramatically. As a result, Steel Partners’ hostile bids failed miserably because they no longer offered a substantial premium to shareholders.⁸⁷ In 2005, after Sotoh’s management decided that the threat of a hostile takeover was no longer imminent they decreased dividends to pre-bid levels.⁸⁸ The tactic used by Sotoh’s management to “pay off” its shareholders with a short-term dividend increase, to maintain their power, is reminiscent of Japanese managers using corporate funds to ‘pay off’ greenmailers in the 1980s.

In 2005, Livedoor’s failed hostile takeover of Nippon Broadcasting System (“NBS”) caused a media circus that rivaled any business story in recent memory.⁸⁹ Public interest in the attempted hostile takeover was fueled by Livedoor’s flamboyant 32-year-old president and university dropout, Takafumi Horie, who became a billionaire and cultural icon through a dotcom company he started named Livin’ on the Edge (later renamed Livedoor).⁹⁰ Horie’s spiky-hair, “Cheshire cat” grin, silver-blue Ferrari, bikini-clad girlfriend and t-shirt and jeans business attire mesmerized the Japanese public.⁹¹ It seemed that Japanese people, especially the younger generation, could not get enough of this brash young entrepreneur taking on Japan’s corporate old guard who had fallen out of favor during the lost decade.⁹²

Experts and academics fell into the “Horie-hype” and pointed to Horie as evidence of a dramatic shift in Japanese corporate governance.⁹³ Some experts posited that the day Horie launched Livedoor’s bid for NBS marked the “advent of an era of hostile takeovers” in Japan.⁹⁴ Other experts claimed that Livedoor’s takeover attempt sparked “a revolution in [Japan’s market for] corporate control.”⁹⁵ Some other experts even erroneously credited Horie with pulling off Japan’s first-ever successful hostile takeover

86 See *Ibid.* 2181; “Hostile Bids are Back Again: Who Should Rejoice?”, *Economist*, 21 February, 2004.

87 See MILHAUPT, *supra* note 3, 2181.

88 COLCERA, *supra* note 48, 113-114

89 See C. ALGER, The Livedoor Looking Glass: Examining The Limits Of Hostile Takeover Bids In Japan, in: *New York University Journal of Law and Business* 3 (2006) 309, 319; GRUENER, *supra* note 4, 878; J. KINGSTON, The Beginning of the End for Japan Inc., in: *International Herald Tribune*, 1 April, 2005.

90 MILHAUPT, *supra* note 3, 2181.

91 “Stirred by Flashy Entrepreneur”, *New York Times*, 19 January, 2006.

92 See KINGSTON, *supra* note 89; “The Battle for Corporate Control: The Outlook for M&A in Japan”, *Economist Intelligence Unit* (2005) 11-13.

93 *ECONOMIST INTELLIGENCE UNIT* 2005, *supra* note 92, 11-13.

94 “Reality check for new-media mirage”, *Weekend Australian*, 21 January, 2006; “Livedoor May Have Opened Door to Era of Hostile Takeovers”, *Japan Economic Newswire*, 23 February, 2005.

95 *ECONOMIST INTELLIGENCE UNIT*, *supra* 92, 7.

before the Livedoor bid was even complete.⁹⁶ In the end, similar to most other trends in Japan, the “Horie-hype” faded quickly.⁹⁷ Livedoor’s hostile bid failed in traditional fashion with stable friendly shareholders coming to NBS’ rescue and Horie being disgraced by an accounting fraud and stock market manipulation conviction that sent him from his Roppongi Hills penthouse to the “Japanese big house.”⁹⁸

All ‘Horie-hype’ aside, the Livedoor case was simply another example of a maverick Japanese investor being defeated by incumbent Japanese management with help from friendly stable shareholders. The Livedoor case arose out of an unusual cross-shareholding relationship that existed between NBS and Fuji TV, which were both part of the same media conglomerate (the Fujisankei Communications Group).⁹⁹ Fuji TV, Japan’s largest private television company, was technically controlled by NBS, a much smaller radio station, by virtue of the fact that NBS owned 22.5 percent of Fuji TV’s shares, while Fuji TV owned only 12.4 percent of NBS’ shares.¹⁰⁰ This created the perverse incentive for corporate raiders to target the much less valuable NBS to gain *de facto* control of Fuji TV.

To rectify this situation, on January 17, 2005, Fuji TV announced an all-cash offer for all of the outstanding shares of NBS. Fuji TV’s bid was below the market price for NBS shares, which (as explained below) was characteristic of takeover bids in Japan prior to and during the lost decade recovery.¹⁰¹ Despite the below market offer, the takeover bid was immediately approved by Fuji TV’s management, which was also predictable during Japan’s lost decade recovery.¹⁰²

However, unbeknownst to NBS and Fuji TV, during the tender offer period, Livedoor was secretly acquiring NBS shares in after-hours trading.¹⁰³ On February 8, 2005, before Fuji TV’s tender offer period had expired, Livedoor made the shocking announcement that it had acquired 29.6 percent of NBS’ shares (bringing its stake up to thirty-eight percent) and intended to acquire the remainder.¹⁰⁴ NBS responded quickly with defensive measures by announcing that it would issue warrants to Fuji TV, which if exercised, would dramatically increase NBS’ share capital by 140 percent and dilute Livedoor’s stake in NBS to less than twenty percent.¹⁰⁵

96 SMITH, *supra* note 42; see CORPORATE VALUE REPORT 2005, *supra* note 29, 14.

97 NIKKEI, *supra* note 43.

98 See ALGER, *supra* note 89, 321; ECONOMIST INTELLIGENCE UNIT, *supra* note 92; “Livedoor Founder Horie Given 2 1/2-Year Prison Term”, Japan Economic Newswire, 16 March, 2007.

99 ALGER, *supra* note 89, 319.

100 *Ibid.*

101 *Ibid.*; ECONOMIST INTELLIGENCE UNIT, *supra* note 92.

102 ECONOMIST INTELLIGENCE UNIT, *supra* note 92.

103 ALGER, *supra* note 89, 319; HINES ET AL., *supra* note 3, 375-376.

104 ALGER, *supra* note 89, 319; MILHAUPT, *supra* note 3, 2179.

105 ALGER, *supra* note 89, 319; GRUENER, *supra* note 4, 879; NAKAMOTO, *supra* note 4.

In response to NBS' defensive actions, Livedoor sought an injunction from the court to stop the issuance of the NBS warrants. The fact that the warrants, if exercised, would have more than doubled NBS' capital made it virtually impossible for NBS to argue convincingly that the "primary purpose" of the issuance was to raise capital and not to entrench management.¹⁰⁶ Therefore, unsurprisingly, in light of the well-established "primary purpose test," the Tokyo District Court granted NBS' injunction, which was affirmed on appeal by the Tokyo High Court.¹⁰⁷

Livedoor's court victory prompted Fuji TV's management to fight back using traditional defensive tactics. Fuji TV called on its friendly stable shareholders to increase their NBS holdings and convinced Softbank Investment to borrow fifteen percent of Fuji TV's shares from NBS—making Softbank Investment Fuji TV's largest shareholder.¹⁰⁸ As a result, Livedoor could no longer gain *de facto* control over the extremely valuable Fuji TV by controlling NBS. In addition, NBS' management received crucial support from its lifetime employees, as ninety percent of them signed a public statement supporting NBS' incumbent management over Horie and Livedoor.¹⁰⁹

In April 2005, in an act that was tantamount to admitting defeat, Livedoor sold its NBS shares to Fuji TV at a marginal profit, which was just enough to allow Horie to "save face."¹¹⁰ In the end, Livedoor was defeated because, in traditional fashion, stable and friendly shareholders rallied around incumbent management, "demonstrating that the era of a truly free stock market [was] still a long way off" in Japan.¹¹¹ In addition, the defeat emphasized that Japan's unique corporate governance, embodied here by lifetime employees, renders dubious any predictions of hostile takeovers that find support from American precedent.

In the year following Livedoor's failed hostile takeover, there were a number of other hostile takeover attempts. These attempts received far less coverage and were universally unsuccessful.¹¹² However, in the summer of 2006, hopeful hostile takeover pundits emerged again when Oji Paper launched its hostile takeover bid for Hokuetsu Paper Mills. Oji's bid reignited familiar claims of an "epoch-making" event that was sure to spark a "wave" of successful hostile takeovers in Japan.¹¹³ Predictably, yet again, Oji's bid failed in traditional fashion with friendly stable shareholders rescuing Hokuetsu's management at the expense of individual minority shareholders.¹¹⁴

106 GRUENER, *supra* note 4, 879.

107 *Ibid.* 878-879; ALGER, *supra* note 89, 320.

108 ECONOMIST INTELLIGENCE UNIT, *supra* note 92, 11-13.

109 *Ibid.*

110 *Ibid.*

111 *Ibid.*; see ALGER, *supra* note 89, 319-321.

112 PUCHNIAK, *supra* note 1, 246.

113 P. ALFORD, Japanese Paper Giants Practise Origami on Corporate Rule Book, in: Australian, 9 August, 2006; NIKKEI, *supra* note 43; "Oji's TOB First by Smokestack Firm, Heralds New M&A Era", Nikkei Weekly, 31 July, 2006.

114 See ALFORD, *supra* note 113; W. PESEK Jr., Japan's Barbarians Within, in: International

The particular facts in the Oji case are worth examining because they illustrate that, even as the lost decade recovery was coming to an end, incumbent Japanese management still maintained an iron grip on their *de facto* corporate control. In May 2006, the event that triggered Oji's unsolicited takeover bid occurred when Hokuetsu decided to expand the production capacity in its Niigata plant, posing a serious threat to profits in Japan's already saturated paper industry.¹¹⁵ On July 3, 2006, in response to this threat, Oji's management informed Hokuetsu that it intended to acquire Hokuetsu and provided its plan for a post-merger integration.¹¹⁶ As expected, Hokuetsu's management quickly began working behind the scenes to rally its friendly and stable shareholders to ward off Oji's unwelcome takeover attempt.¹¹⁷

On July 21, 2006, Hokuetsu's board put its defensive measures into action. The board decided that it would issue Mitsubishi, a friendly stable shareholder, 50 million shares at the discount price of 607 yen—which was approximately five percent below the previous closing price and ten percent below the high earlier in the year.¹¹⁸ The share issuance would provide Mitsubishi with a twenty-four percent stake in Hokuetsu's expanded capital and ensure that Hokuetsu's management had a large block of stable friendly shares to protect them against Oji's attempted hostile takeover.¹¹⁹ At the same meeting, the board voted itself a poison pill in the form of equity warrants issued to friendly stable shareholders, including Mitsubishi, which were exercisable in the event that Oji (or any other unwelcome acquirer) made an unsolicited tender offer.¹²⁰

As to be predicted, Hokuetsu's defensive measures ensured the entrenchment of Hokuetsu's incumbent management, but blatantly disregarded minority shareholders. Without a seat on Hokuetsu's board, the average shareholder would have had no way of knowing that twenty-four percent of their company had been offered to Mitsubishi at a significant discount, that they were to be diluted by sixteen percent, and that a new poison pill protected management.¹²¹ Minority shareholders also received scant protection from the so-called "independent committee"¹²² that approved the poison pill, as it was made up of two retired auditors who had previously worked for Hokuetsu and a

Herald Tribune, 6 August, 2006.

115 ALFORD, *supra* note 113.

116 See K. OSUGI, What is Converging? Rules on Hostile Takeovers in Japan and the Convergence Debate, in: Asian-Pacific Law & Policy Journal 9 (2007) 143; "TOB 'Hostility' Limited by Tradition", Nikkei Weekly, 4 September, 2006; C. WRIGHT, Hostile Bid Subverts Japanese Politeness, in: Euromoney, September 2006.

117 ALFORD, *supra* note 113.

118 ALFORD, *supra* note 113; M. SANCHANTA, Oji Paper Gives Up on Hokuetsu Takeover, in: Financial Times, 6 September, 2006.

119 ALFORD, *supra* note 113.

120 *Ibid.*

121 *Ibid.*

122 HINES ET AL., *supra* note 3, 412-413.

Shinto priest—hardly a model for minority shareholder protection.¹²³ The TSE was similarly left in the dark by Hokuetsu's management-dominated board, which conveniently failed to mention Oji's takeover offer when it gave notice to the TSE (as required by the New TSE Listing Rules) about the board's plan to institute the poison pill.¹²⁴

Finally, on July 23, 2006, after spending more than two weeks surreptitiously building an impenetrable barrier of takeover defenses, Hokuetsu's management formally rejected Oji's takeover offer.¹²⁵ Oji's president responded by publicly announcing that if Hokuetsu cancelled its planned placement of shares with Mitsubishi, Oji would make an on-market offer for 50.1 percent of Hokuetsu's shares at the premium price of 860 yen—thirty-five percent above the previous closing price.¹²⁶ The stock market quickly responded to Oji's potential offer by driving up Hokuetsu's shares to 825 yen.¹²⁷

At this point, from an American shareholders' rights perspective, the planned placement by Hokuetsu's board of a quarter of the company with Mitsubishi for 607 yen per share, which now stood at a whopping twenty-six percent discount to the current market price, appeared unthinkable.¹²⁸ However, Hokuetsu's board would make its decision in Tokyo, not Delaware. So predictably, the placement of Hokuetsu's shares in Mitsubishi went through as planned.

Then, when it seemed that the shenanigans of Japanese management could not get any worse, Oji was blindsided again when Nippon Paper Group announced that it had acquired an 8.5 percent stake in Hokuetsu to help block the Oji bid.¹²⁹ Even more shocking, Nippon Paper's management-dominated board paid approximately 800 yen for the same shares that Mitsubishi was being handed for 607 yen—knowing full well that when Hokuetsu placed its shares with Mitsubishi it would significantly dilute Nippon Paper's stake.¹³⁰ For good measure, Nippon Paper's board also conveniently forgot to comply with the five percent reporting rule when it acquired its 8.5 percent blocking stake in Hokuetsu.¹³¹

This is where claims that Japan's hostile takeovers market dramatically changed during the lost decade recovery begin to unravel.¹³² According to such claims, in the dramatically changed environment of the lost decade recovery, Japanese shareholders

123 ALFORD, *supra* note 113; "Barbarians Within the Gate", *Economist*, 12 August, 2006.

124 ALFORD, *supra* note 113.

125 NIKKEI WEEKLY, 2006, *supra* note 116.

126 ALFORD, *supra* note 113; WRIGHT, *supra* note 116.

127 ALFORD, *supra* note 113.

128 *Ibid.*; *ECONOMIST*, *supra* note 123.

129 *ECONOMIST*, *supra* note 123.

130 ALFORD, *supra* note 113.

131 *Ibid.*

132 There have been a myriad of claims from experts that Japan developed a vigorous, American-style, hostile takeovers market during the recent recovery. See, PUCHNIAK, *supra* note 1, footnote 343.

should have challenged Hokuetsu's unreasonable defensive measures in court.¹³³ Conversely, Hokuetsu's friendly shareholders should not have sacrificed shareholder value in their own companies merely to save Hokuetsu's incumbent management. In Milhaupt's words, during the lost decade recovery it was "no longer considered acceptable [for Japanese boards]....to support incumbent management....regardless of the financial consequences to their own shareholders".¹³⁴ Based on such claims, there should have been a tirade of litigation challenging the "Shinto priest approved" poison pill; the sale of a quarter of Hokuetsu to Mitsubishi at an unreasonable discount; and the purchase of soon-to-be-diluted shares at an unjustifiable premium by Nippon Paper's management-dominated board.¹³⁵

However, what "should have" happened, based on the predictions of hopeful hostile takeover pundits, did not. There was not a single legal proceeding commenced in the Oji-Hokuetsu case.¹³⁶ The brazen defensive measures by Hokuetsu's management and its friendly stable shareholders produced not a peep from nascent shareholders. Even Hokuetsu's foreign shareholders, who held twenty-five percent of the company, would not take the risk of challenging the defensive measures of Hokuetsu's corporate old guard.¹³⁷

Finally, on August 30, 2006, without a legal action in sight, over thirty percent of Hokuetsu in the hands of two companies that were not on the share register a month before, and with a "Shinto priest approved" poison pill in place, Oji conceded defeat.¹³⁸ Oji's "epoch-making" bid for 50.1 percent of Hokuetsu, which received rave reviews from the international business community for making impeccable business sense, managed to net Oji a paltry 5.25 percent of Hokuetsu's shares—not exactly a menacing threat to Hokuetsu's entrenched management.¹³⁹ However, Oji's hostile attempt did achieve one thing. It made Oji a pariah in Japan's "old school" paper industry and left the Japanese bank that supported Oji's bid wondering why it ever went out on a limb to do so.¹⁴⁰

The Oji case occurred as Japan's remarkable 5-year lost decade recovery was ending and its economy was transitioning into what appeared to be an era of sustained growth—before it was derailed by the global financial crisis. This example clearly illustrates that not much changed during the lost decade recovery as hostile takeovers continued to play a marginal role in corporate restructuring.¹⁴¹ This is confirmed by a survey of Japanese

133 See MILHAUPT, *supra* note 3, 2202.

134 *Ibid.* 2186.

135 ALFORD, *supra* note 113.

136 See *Ibid.*

137 See WRIGHT, *supra* note 116.

138 See "Oji / Hokuetsu", *Financial Times*, 30 August, 2006.

139 SANCHANTA, *supra* note 118; see also "Under Pressure", *Economist*, 9 September, 2006.

140 See WRIGHT, *supra* note 116; NIKKEI, *supra* note 43.

141 See WRIGHT, *supra* note 116.

management shortly after the Oji bid, which reported that seventy-seven percent of Japanese executives said that they would not consider attempting a hostile takeover.¹⁴² However, in the same survey, ninety-three percent expected friendly corporate acquisitions to continue to increase in Japan.¹⁴³ This suggests that the “efficiency of friendliness,” which drove the lost decade recovery, will likely continue to be the *modus operandi* in Japanese corporate governance for the foreseeable future. Indeed, since Oji’s bid failed, friendly takeovers have persisted and Japan remains the only developed country in which there has yet to be a successful hostile takeover bid.¹⁴⁴

V. THE INCREASE IN JAPANESE TAKEOVER *BIDS* IS NOT EVIDENCE OF AN INCREASE IN THE *EX ANTE* THREAT OF HOSTILE TAKEOVERS

A technical point that must be addressed before moving on is the claim by some experts that an increase in the number of takeover bids in Japan during the lost decade and lost decade recovery demonstrates that Japan developed, or was developing, an American-style hostile takeovers regime.¹⁴⁵ This claim would be accurate if takeover bids in Japan were tantamount to takeover bids in the United States. However, they are not. The significant discrepancy between what is considered a takeover bid in Japan and the United States makes conclusions based on comparisons between them erroneous.

In the United States, the number of takeover bids has come to be viewed as a proxy for the threat level of hostile takeovers.¹⁴⁶ This is because, contrary to mergers, takeover bids allow bidders to bypass management by making an offer directly to target shareholders.¹⁴⁷ This allows takeover bidders to assume control of target companies without management’s approval (i.e., via a hostile takeover) and then to replace unskilled or underperforming management to improve company performance.¹⁴⁸

142 “Top Execs Split on Approval for Oji’s Run at Hokuetsu”, *Nikkei Weekly*, 11 September, 2006.

143 *Ibid.*

144 In fact, the most recent significant failed attempted hostile takeover involved the high profile failure of Steel Partners to take over Bulldog Sauce. OSUGI, *supra* note 116, 158-159; NELS HANSEN, Japan’s First Poison Pill Case, Bulldog Sauce vs. Steel Partners: A Comparative and Institutional Analysis, in: *Journal of Japanese Law* 26 (2008)139. In addition, at the end of 2007, there were renewed claims that Japan had just experienced its “first hostile takeover.” Again, these claims were overly exaggerated and ultimately false. See “Hostility, of Sorts”, *Economist*, 22 December, 2007.

145 COLCERA, *supra* note 48, 48-52; SCHAEDE, *supra* note 4, 22; SCHAEDE, *supra* note 41, 32.

146 See D.G. BAIRD / R.K. RASMUSSEN, Private Debt and the Missing Lever of Corporate Governance, in: *University of Pennsylvania Law Review* 154 (2006) 1243; B. HOLMSTROM / S.N. KAPLAN, Corporate Governance and Merger Activity in the United States: Making Sense of the 1980s and 1990s, in: *The Journal of Economic Perspectives*, 15 (2001) 125.

147 BURKART / PANUNZI, *supra* note 4, 2.

148 *Ibid.* 3.

During the vigorous hostile takeovers market in 1980s America, takeover bids were the primary means for initiating and executing hostile takeovers.¹⁴⁹ In the 1980s, the United States was an epicenter for hostile takeovers, as over half of all major American companies received hostile takeover bids.¹⁵⁰ In 1988 alone, there were over 200 hostile takeover bids and 85 successful hostile takeovers.¹⁵¹ As such, during the 1980s, the threat of a hostile takeover bid and a subsequent overhaul of management was a real prospect for every CEO of a listed American company. Many experts claim that, in the late 1980s, this *ex ante* threat of being subject to a hostile bid, with the real prospect of being taken over, forced American executives to focus on maximizing shareholder value and reducing agency costs, which successfully drove the restructuring of corporate America.¹⁵²

In Japan, prior to 1990, there were virtually no takeover bids.¹⁵³ From 1990 until 1997, takeover bids increased modestly to less than 10 bids per year. However, since 1997, there has been a substantial increase in the number of takeover bids from about 20 in 1999, 30 in 2001, 40 in 2004, and 50 in 2005.¹⁵⁴ According to American precedent, this increase in takeover bids should have significantly increased the threat of hostile takeovers in Japan. Indeed, several experts have pointed to the increase in the number of takeover bids as evidence that the threat of hostile takeovers significantly increased in Japan during the lost decade and lost decade recovery.¹⁵⁵

However, comparing Japanese and American takeover bids is like comparing “apples and oranges.” Compared to their American counterparts, Japanese takeover bid rules are extremely broad.¹⁵⁶ In Japan, with only a few limited exceptions, a proposed purchase of shares will be considered a takeover bid whenever shares are acquired outside of the securities market.¹⁵⁷ In the United States, for a proposed purchase of shares to be considered a takeover bid it generally must meet eight criteria including that the offer price is higher than the market price (i.e., the offer includes a ‘premium’).¹⁵⁸

149 *Ibid.* 1.

150 HOLMSTROM / KAPLAN, *supra* note 146, 125.

151 M. MARTYNOVA/L. RENNEBOOG, Takeover Waves: Triggers, Performance and Motives, in: ECGI Finance Working Paper No. 97 (2005) 8, <http://ssrn.com/abstract=880379>.

152 M.J. ROE, Political Preconditions to Separating Ownership from Corporate Control, in: Stanford Law Review 53 (2000) 539, 558; see also BURKAT / PANUNZI, *supra* note 4, 9, 24; HOLMSTROM / KAPLAN, *supra* note 146, 125.

153 KESTER, *supra* note 10, 99; C.J. MILHAUPT / M.D. WEST, Institutional Change and M&A in Japan: Diversity Through Deals, 2001, 36 (forthcoming in C.J. MILHAUPT, Global Markets, in: Domestic Institutions), <http://papers.ssrn.com/abstract=290744>.

154 COLCERA, *supra* note 48, 49.

155 SCHAEDE, *supra* note 4, 22-26.

156 K. KOMOTO, The Present Status of Takeover Bids (TOB) and Their Effect on Stock Prices, in: NLI Research No.147 (2000) 8-9, <http://www.nli-research.co.jp/english/economics/2000/eco0012a.pdf>.

157 *Ibid.*

158 D.A. OESTERKE, The Rise and Fall of Street Sweep Takeovers, in: Duke Law Journal 1989,

According to two studies conducted on takeover bids in Japan in the post-bubble era, almost half of the takeover bids had an offer price below the market price (i.e., a “negative premium”).¹⁵⁹ Therefore, on this basis alone, half of the post-bubble takeover bids would not be considered takeover bids under United States law. More importantly, these negative premium bids present absolutely no *ex ante* threat to management to maximize shareholder value or control agency costs. To the contrary, management may feel they can allow the company’s share price to decline if there are negative premium bids in the market.

A related peculiarity in Japanese takeover bids is that the average premium offered to shareholders was (and is) extremely low compared to the premium offered to shareholders in American takeover bids (and in bids in all other countries). In the United States, the average premium offered to shareholders in takeover bids is about forty-five percent above the market price.¹⁶⁰ In Japan, during the lost decade, the average premium offered to shareholders in takeover bids was *minus* 4.72 percent.¹⁶¹ According to one study that examined takeover bids from 1990 to 2002, Japan held the unique distinction of being the *only* country in the world that had an average *negative* bid premium.¹⁶² Even during the lost decade recovery, when premiums were said to have increased, the average premium offered was a modest ten percent, which is well below the forty-five percent offered in the United States.¹⁶³

Takeover bid premiums in Japan were considerably lower than in the United States (and all other developed countries) because a significant portion of Japanese takeover bids involved friendly pre-negotiated deals between bidders and target companies.¹⁶⁴ In these so-called “takeover bids,” the offer price is arranged between the acquirer and main shareholders (with approval from ‘target’ management) prior to the offer being made and there is no competition between potential acquirers. This is in sharp contrast to American takeover bids where prearranged friendly offers to a single bidder, which normally have a small or negative premium, are not considered takeover bids.¹⁶⁵ These low premium prearranged takeovers, which predominated in Japan during the lost decade and lost decade recovery, do nothing to increase the threat of hostile takeovers. In fact, they are welcomed by incumbent management as they may present an oppor-

202, footnote 92.

159 KOMOTO, *supra* note 156, 10; MILHAUPT / WEST, *supra* note 153, 17.

160 S. ROSSI / P.F. VOLPIN, Cross-Country Determinants of Mergers and Acquisitions, in: *Journal of Financial Economics* 74 (2004) 282.

161 MILHAUPT / WEST, *supra* note 153, 17.

162 ROSSI / VOLPIN, *supra* note 160, 282.

163 See H. MIYAJIMA, Analyzing the Role of M&As for Japanese Companies, in: RIETI Report No. 076 (2006), http://www.rieti.go.jp/en/rieti_report/076.html; ROSSI / VOLPIN, *supra* note 160, 282.

164 KOMOTO, *supra* note 156, 11.

165 *Ibid.* 10.

tunity to be rescued from hidden liabilities (which may be the reason for the negative premium bids) that have not been disclosed to the market.¹⁶⁶

Even the rare Japanese takeover bids that included premiums similar to typical American takeover bids have failed.¹⁶⁷ Again, this is in contrast to the United States, where about thirty-five percent of hostile bids succeed, and the European Union, where fifty percent of hostile bids are successful.¹⁶⁸ Obviously, with a zero percent success rate, even takeover bids that do offer a substantial premium, will not pose the same level of threat as takeover bids in the United States or European Union, where there is a significant chance that a takeover bid will result in a successful hostile takeover.

Finally, even if all of the significant differences between Japanese and American takeover bids are ignored, the total number of takeover bids in the United States during the late 1980s still dwarfs the number in Japan during the lost decade and lost decade recovery. In the United States, during the last five years of the 1980s, there was approximately three times the number of takeover bids as in Japan during the lost decade and lost decade recovery—which lasted over 15 years.¹⁶⁹ Of course, this overlooks a significant percentage of so-called Japanese “takeover bids” which were not a proxy for hostility in the market.

In sum, it is undeniable that there was an increase in takeover bids in Japan during the lost decade and lost decade recovery. However, this increase is not comparable to that of the United States in the 1980s—in either the nature or frequency of the bids. This is because a significant percentage of Japanese “takeover bids” were friendly, negotiated deals with low or negative premiums. In addition, all of the bids offering premiums equivalent to those in the United States failed. As such, the raw number of so-called “takeover bids” in Japan during the lost decade and lost decade recovery is not a reliable proxy for the threat of hostile takeovers. If anything, especially during the lost decade, it is more likely that Japanese takeover bids acted as a proxy for perversity in the market (i.e., stronger companies rescuing weaker ones with undisclosed liabilities, which may explain negative premium bids) than as threats of hostile takeovers.¹⁷⁰

166 *Ibid.* 12-13.

167 *Ibid.* 12.

168 CORPORATE VALUE REPORT 2005, *supra* note 29, 12.

169 PUCHNIAK, *supra* note 1, footnote 381.

170 See D.W. PUCHNIAK, Perverse Main Bank Rescue in the Lost Decade: Proof that Unique Institutional Incentives Drive Japanese Corporate Governance, in: Pacific Rim Law & Policy Journal 16 (2007) 13, 20-24.

VI. JAPANESE MANAGERS DID NOT REACT SWIFTLY TO THE PURPORTED THREAT OF FAILED HOSTILE TAKEOVERS

Another way to gauge the effect of failed hostile takeovers on corporate governance during the lost decade recovery is to attempt to measure the subjective threat felt by Japanese managers as a result of failed hostile takeovers. From a corporate governance perspective, the threat of hostile takeovers only becomes significant if it is serious enough to influence managerial behavior.¹⁷¹ A clear indication that management perceives the threat of hostile takeovers as serious is when management takes steps to protect itself against hostile takeovers. During the 1980s, the serious threat of hostile takeovers in the United States drove managers to take a number of defensive actions. Two of the most significant actions were adopting poison pills and increasing the prominence of independent directors on American boards—both of which were effective in guarding against hostile takeovers.¹⁷²

In November 1985, the Delaware Supreme Court upheld a company's right to adopt the poison pill as a takeover defense.¹⁷³ Shortly after the court's "authorization of the pill," over 1000 American companies adopted this defensive technique. Furthermore, by the mid-1990s, over sixty percent of all listed American companies had adopted the pill.¹⁷⁴ This is definitive evidence that, in the late 1980s, the threat of hostile takeovers was serious enough to drive managerial action in the majority of American companies.

Prior to 2001, the poison pill was not available under Japanese law. In 2001, a *Commercial Code* amendment made a version of the poison pill technically available in Japan.¹⁷⁵ However, despite efforts by large law firms to market the pill and predictions by experts that the pill may be widely adopted, no Japanese companies adopted it.¹⁷⁶

171 MIYAJIMA / KUROKI, *supra* note 41, 79 and 85.

172 R. MONKS / N. MINOW, *Corporate Governance*, (3d ed., 2004) 227, 248; see also BAIRD / RASMUSSEN, *supra* note 146, 1244; L.A. BEBCHUK / A. COHEN, *The Costs of Entrenched Boards*, in: *Journal of Financial Economics* 78 (2005) 409, 410; L.A. BEBCHUK ET AL., *The Powerful Anti-takeover Force of Staggered Boards: Theory Evidence and Policy*, in: *Stanford Law Review* 54 (2002) 887, 895; GILSON, *supra* note 4, 33-34; GRUENER, *supra* note 4, 873.

173 *Moran v. Household Int'l. Inc.*, 500 Atlantic Reporter 1346 (Delaware Supreme Court 1985); see generally GILSON, *supra* note 4, 33-34.

174 BEBCHUK / COHEN, *supra* note 172, 413; MONKS / MINOW, *supra* note 172, 237.

175 C.J. MILHAUPT, *A Lost Decade for Japanese Corporate Governance Reform?*, in: *The Center for Law and Economic Studies, Working Paper Series No. 234* (Columbia Law School, 2003), footnote 24, <http://ssrn.com/abstract=442960>. See also, S. KOZUKA, *The Use of Stock Options as Defensive Measures: The Impact of the 2001 Amendments to the Corporate Law on Corporate Controls in Japan*, in: *Journal of Japanese Law* 15 (2003) 135.

176 See GILSON, *supra* note 4, 23-24; C.J. MILHAUPT, *Foreword To The Hostile M&A Conference Issue*, in: *Columbia Business Law Review* 2004, 1, 5-7; H. KANDA, *Does Corporate Law Really Matter In Hostile Takeovers?: Commenting on Professor Gilson and Chancellor Chandler*, in: *Columbia Business Law Review* 2004, 75; Z. SHISHIDO, *Changes in Japanese Corporate Law and Governance: Revisiting the Convergence Debate*, in: *Law and Econo-*

This failure to adopt the pill may have been because, although it was technically available, its legal status was still uncertain.¹⁷⁷

Then, in 2005, the government responded to the uncertainty of the legality of the poison pill by releasing the Takeover Guidelines which “officially sanctioned” the poison pill and imported Delaware takeover jurisprudence into Japan.¹⁷⁸ Both the government and large law firms actively encouraged listed companies to adopt the “officially sanctioned” poison pill.¹⁷⁹ Based on American experience in the 1980s, it was assumed that “officially sanctioning” the pill would cause a wave of companies to adopt it.¹⁸⁰ Central to this assumption was the erroneous belief that Japanese managers were seriously threatened by hostile takeovers during the lost decade recovery—regardless of the fact that all hostile takeover bids had failed.

However, despite the 2001 *Commercial Code* amendment, the “official sanctioning” of the pill, and the government and law firms’ attempts to market the pill, the adoption of the pill during the lost decade recovery was, at best, “limited and gradual”.¹⁸¹ In 2005, only eight out of Japan’s 4,000 listed companies adopted the poison pill at their annual general shareholders’ meeting.¹⁸² Even by 2006, as the lost decade recovery ended and what was to be Japan’s period of sustained growth commenced, still less than two percent of Japan’s listed companies had adopted the pill.¹⁸³ In sum, during the lost decade recovery, very few Japanese managers feared hostile takeovers enough to implement the poison pill. This empirical evidence also calls into question predictions by experts who expected Japan to rush to adopt the pill based on the past experience in American corporate governance during the 1980s.¹⁸⁴

mics Workshop, Paper 1 (University of California Berkeley 2004) 11-12, http://repositories.cdlib.org/berkeley_law_econ/Fall2004/1/.

177 KANDA, *supra* note 176, 70-71; MILHAUPT, *supra* note 176, 5.

178 See MILHAUPT, *supra* note 3, 2173-2174 and 2200.

179 See *ibid.* 2206-2208; see also ECONOMIST, *supra* note 139.

180 See HINES ET AL., *supra* note 3, 374-375; MILHAUPT, *supra* note 3, 2200-2201; SCHAEDE, *supra* note 4, 24-25.

181 GRUENER, *supra* note 4, 873-874; HINES ET AL., *supra* note 3, 408.

182 GRUENER, *supra* note 4, 873; OSUGI, *supra* note 116.

183 According to the Ministry of Economy, Trade and Industry, by March 2006, 48 companies had introduced the poison pill out of Japan’s approximately 4000 listed companies. Corporate Value Study Group, Corporate Value Report 2006, 7, footnote 7, http://www.meti.go.jp/policy/economic_oganzation/pdf/houkoku06. For a summary of the Corporate Value Report 2006, see Corporate Study Group, Corporate Value Report 2006 (Abstract), in: Journal of Japanese Law 21 (2006) 140. There are reports that, by the end of 2007, slightly less than ten percent of listed companies had adopted the poison pill. OSUGI, *supra* note 116, 158. However, in the context of this paper, adoption of the pill after the end of the lost decade recovery (i.e., mid-2006) is irrelevant because it tells us nothing about the *ex ante* threat of hostile takeovers *during* or *preceding* the recent recovery—which is what this paper focuses on.

184 See MILHAUPT, *supra* note 3, 2200; CANADIAN INVESTOR RELATIONS INSTITUTE, The Year of the Poison Pill (August 2005), http://www.ciri.org/resources/reading_room/articles/shareholder/?article_id=953.

Also in the 1980s, the rise of the poison pill in the United States was accompanied by an increase in the prominence of independent directors on American boards.¹⁸⁵ Delaware jurisprudence made the independence of boards a central criterion for justifying the appropriateness of defensive actions taken in response to hostile takeover bids.¹⁸⁶ This resulted in a significant increase in the number and quality of independent directors on American boards as management attempted to insulate themselves from the serious threat of hostile takeovers.¹⁸⁷

In 2002, the *Commercial Code* was amended to allow Japanese companies to opt out of the traditional Japanese-style board featuring the statutory auditor and to adopt instead an American-style board with an “independent committee system.”¹⁸⁸ Firms that opted for the American-style board were required to establish “independent” board committees for the audit, nomination, and compensation functions, which take the place of the statutory auditor.¹⁸⁹ A key element of the American-style board is that it legally mandates a separation between directors and executive officers, which is synonymous in the traditional Japanese-style statutory auditor system.¹⁹⁰

The combination of the separation between directors and executive officers and the increased independence of the committee system should have made American-style boards an attractive option for companies that felt threatened by hostile takeovers because it increased their ability to justify the adoption of takeover defenses. This was especially true after the release of the 2005 Takeover Guidelines, which transplanted Delaware takeover jurisprudence into Japan. Indeed, after the Takeover Guidelines were released, Milhaupt predicted “there could be a spike in adoptions of the U.S.-style board committee system” because the independent committees played a large role in Delaware takeover jurisprudence.¹⁹¹

Milhaupt’s prediction proved to be incorrect. In fact, the opposite has happened. Since 2002, less than three percent of Japan’s listed companies have chosen to adopt an American-style board.¹⁹² In addition, over three-quarters of the companies that have adopted an American-style board did so in 2003 (the year following the amendment).¹⁹³ Thus, the number of companies that decided to adopt the American-style board was considerably lower after the Takeover Guidelines were implemented in 2005 than in 2002,

185 GILSON, *supra* note 4, 33-34; MONKS / MINOW, *supra* note 172, 227, 248.

186 GILSON, *supra* note 4, 34.

187 MONKS / MINOW, *supra* note 172, 227, 248; see also GILSON, *supra* note 4, 33-34.

188 See D.W. PUCHNIAK, The 2002 Reform of the Management of Large Corporations in Japan, in: *Australian Journal of Asian Law* 5 (2003) 42, 46.

189 See *ibid.* 49-56; MILHAUPT, *supra* note 3, 2187.

190 See MILHAUPT, *supra* note 3, 2187; PUCHNIAK, *supra* note 188, 50, 55-56.

191 MILHAUPT, *supra* note 3, 2202.

192 P. LAWLEY, Panacea or Placebo? An Empirical Analysis of the Effect of the Japanese Committee System Corporate Governance Law Reform, in: *Asian-Pacific Law & Policy Journal* 9 (2007) 106; OSUGI, *supra* note 116, 158.

193 LAWLEY, *supra* note 192.

after the amendment was first introduced.¹⁹⁴ The fact that so few listed companies have chosen to adopt this change, especially after the Takeover Guidelines imported Delaware takeover jurisprudence, illustrates that the threat of hostile takeovers during the lost decade recovery was not serious enough to influence the actions of the vast majority of Japanese managers.

The failure of Japanese companies to adopt quickly the poison pill and the American-style board is even more of a surprise, considering that 2003 witnessed a postwar low in cross-shareholding and a postwar high of foreign shareholding and shareholder activism. The most logical explanation for the failure of Japanese companies to implement quickly these defensive tactics is that managers did not perceive the threat of hostile takeovers as serious enough to take action. The flawed predictions of a rush to the poison pill and American-style boards should serve as yet another reminder that Japanese corporate governance cannot be understood based on United States' precedent—especially the American hostile takeovers environment of the 1980s.

VII. JAPAN'S "BARRIERS" TO HOSTILE TAKEOVERS BEGAN TO REBUILD DURING THE LOST DECADE RECOVERY

Interestingly, in spite of the litany of predictions that the lost decade recovery would produce a US-style market for corporate control, it in fact produced the opposite—a rebuilding of Japan's traditional barriers to hostile takeovers. The lost decade recovery saw a dramatic return to cross-shareholding.¹⁹⁵ Since 2004, shares held by non-financial companies, which are commonly seen as cross-shareholdings, have rapidly expanded by over thirty percent and the three mega-banks have increased their cross-shareholdings.¹⁹⁶ The return to cross-shareholding, which occurred at the same time the Japanese economy was returning to economic normalcy (prior to the global financial crisis), suggests that Japanese companies sold their cross-shareholdings during the lost decade out of a necessity to raise capital—not because they thought the main bank system or cross-shareholding was fundamentally flawed.¹⁹⁷ It is also worth noting that the recent growth in cross-shareholding occurred despite the fact that the poison pill was “officially sanctioned” by the Japanese government. This calls into question the claim by Milhaupt

194 *Ibid.*

195 See Y. TAKI ET AL., Options Available for Japanese Companies in a Globalized Market Environment, in: NRI Papers No. 111 (2006) 5, <http://www.nri.co.jp/english/opinion/papers/2006/pdf/np2006111.pdf>; W. PESEK, Welcome Back, Japan Inc., in: New York Sun, 19 September, 2006; “Cross-holding Revives as Takeover Shield”, Nikkei Weekly, 29 January, 2007.

196 NIKKEI, *supra* note 195.

197 KANDA, *supra* note 176, 70.

and West that cross-shareholding existed in Japan because Japan's corporate law did not allow for American-style defenses—particularly the poison pill.¹⁹⁸

As the lost decade recovery ended, reports of enthusiasm for hostile takeovers in corporate Japan also waned and even reversed course.¹⁹⁹ In 2005, during Livedoor's hostile takeover attempt, Horie, the founder and CEO of Livedoor, was perceived by a large portion of the Japanese public as the face of Japan's rapidly evolving business culture.²⁰⁰ His hostile attempt to take over Fuji TV was viewed as evidence that American-style hostile takeovers had finally arrived in Japan.²⁰¹ As explained above, even in the wake of Livedoor's failure, many pundits erroneously viewed Horie's mere attempt to challenge the Japanese old guard as a watershed moment marking the beginning of an era of hostile takeovers in Japan.²⁰²

However, in 2006, all of this quickly changed when Horie was arrested and indicted on allegations of accounting fraud and stock market manipulation.²⁰³ The scandal spurred a massive two-day sell-off on the TSE. The volume of selling was so great that the TSE was forced to close early, a move that was seen as a "blow to the nation's pride."²⁰⁴ This caused markets around the world to fall and was dubbed by the news media as the "Livedoor shock."²⁰⁵ Horie was disgraced, as Livedoor's share price plummeted in a month from 696 yen to 61 yen and in April, the stock was delisted from the TSE.²⁰⁶

The picture of Horie solemnly bowing before a trial judge in Tokyo, with his trademark spiky-hair fully cropped and wearing a conservative "salary man" black suit, was a stark contrast to the once renegade shareholder activist who was famous for flamboyantly challenging Japan's conservative business culture.²⁰⁷ In March 2007, Horie was sentenced to two and a half years in prison. Given that Japanese courts rarely impose jail terms for securities violations, many viewed this sentence as extremely harsh.²⁰⁸

198 See HINES ET AL., *supra* note 3, 374-375; MILHAUPT, *supra* note 3, 2173-2174; MILHAUPT / WEST, *supra* note 153, 22, 47.

199 See OSUGI, *supra* note 116, 156-157; see also ALFORD, *supra* note 113; D. IBISON, Koizumi Drops FDI Pledge on M&A Fears, in: Financial Times, 2 February, 2006; ECONOMIST, *supra* note 139.

200 HINES ET AL., *supra* note 3, footnote 227.

201 *Ibid.* 376-77; GRUENER, *supra* note 4, 873 and 895; ECONOMIST INTELLIGENCE UNIT, *supra* note 92, 7.

202 See CARYL, *supra* note 4; KINGSTON, *supra* note 89; NAKAMOTO, *supra* note 4. See more generally, WHITTAKER / HAYAKAWA, *supra* note 48, 5.

203 OSUGI, *supra* note 116.

204 "Stirred by Flashy Entrepreneur", New York Times, 19 January, 2006.

205 ALGER, *supra* note 89, 323.

206 HINES ET AL., *supra* note 3, footnote 227.

207 M. NAKAMOTO, Ex-Livedoor Chief Horie Pleads Not Guilty, in: Financial Times, 5 September, 2006.

208 JAPAN ECONOMIC NEWSWIRE, *supra* note 98; "Livedoor Internet Guru Jailed for Faking Profits", Evening Standard, 16 March, 2007.

Murakami, the CEO of MAC, who was the other *de facto* leader of shareholder activism in Japan during the recent recovery, was also disgraced by criminal charges. In June 2006, Murakami was arrested on allegations of insider trading that took place during the infamous Livedoor hostile takeover attempt.²⁰⁹ As Murakami awaited trial, most commentators saw the case against him as weak but nevertheless expected that he may receive a harsh sentence to send a message to “all those wannabe [corporate raiders] to reassess their approach to the market.”²¹⁰ As suspected, on July 19, 2007, Murakami received the harshest sentence for insider trading ever issued by a Japanese court.²¹¹ During the sentencing, the judge called Murakami’s “profit first attitude . . . horrifying.”²¹²

The imprisonment and disgrace of Japan’s two most prominent shareholder activists, who were widely viewed as the face of hostile takeovers in Japan, has caused a “chilling effect” in Japan’s takeover market.²¹³ Combined with the rise in cross-shareholding, these sentences serve as yet another caution for those who, for the last two decades, have been perpetually predicting the arrival of American-style hostile takeovers in Japan.²¹⁴ They further illustrate how Japan’s unique form of corporate governance continues to persist and dominate.

VIII. CONCLUSION

The lesson from Japan’s lost decade recovery is simple. Hostile takeovers play a marginal role in Japanese corporate governance. This has been the case throughout the postwar period. The lost decade recovery was no exception.

The magnitude of the distorted literature which creates the false impression that hostile takeovers have come to play an important role in Japanese corporate governance is somewhat curious. It is surprising to see one capable scholar after another, over a period of decades, repeat the same mistake by erroneously predicting the arrival of American-style hostile takeovers in Japan. The mantra that global corporate governance will inevitably evolve towards the “optimally efficient” American model appears to have made otherwise bright and careful scholars have “delusions of hostility”.

Hopefully, this article will cure such delusions. After all, correctly understanding the reality of Japan’s unique system of corporate governance is far more enriching than toiling to reconstruct the Japanese facts to fit a preconceived notion of what good corporate governance ought to be.

209 A. FUKUDA, Japanese Investors Face Stricter Disclosure Rules, in: International Herald Tribune, 28 December, 2006.

210 S. HERMAN, Latest Shot Fired In Battle Between Japan Inc., in: United States Federal News, 13 June, 2006.

211 See “Murakami Gets 2-yr Term”, Daily Yomiuri, 20 July, 2007.

212 See *ibid.*

213 HERMAN, *supra* note 210.

214 ECONOMIST INTELLIGENCE UNIT, *supra* note 92, 27.

ZUSAMMENFASSUNG

Die meisten Unternehmensrechtler und Ökonomen mit einem Interesse an der Art und Weise, wie die Corporate Governance in Japan strukturiert ist, gehen davon aus, dass sich unvermeidlich (auch) in Japan ein Markt für Unternehmenskontrolle durch feindliche Übernahmen nach US-amerikanischen Vorbild entwickeln wird. Diese Annahme hat jüngst erneut Auftrieb erfahren, als eine Reihe prominenter Experten fragwürdige Vergleiche zwischen der von ihnen behaupteten Rolle, die feindliche Übernahmeveruche bei der Erholung der japanischen Wirtschaft zwischen 2002 und 2007 nach dem sog. „verlorenen Jahrzehnt“ gespielt haben sollen, und derjenigen, die feindlichen Übernahmen zweifelsfrei bei der wirtschaftlichen Restrukturierung in den USA gegen Ende der 1980er Jahre zukam, aufgestellt haben. In der einschlägigen Literatur ist durch die rätselhafte Fixierung auf die Vorhersage feindlicher Übernahmen für Japan und die schiefen Vergleiche, die zu deren Begründung herangezogen wurden, der falsche Eindruck erweckt worden, diese wären inzwischen zu einem wichtigen Instrument (auch) der japanischen Corporate Governance geworden. Das Gegenteil ist indes der Fall, diese spielen in Japan nach wie vor fast keine Rolle.

Der Beitrag versucht, die so entstandene Verfälschung zu korrigieren. Er deckt anhand von Fallstudien und empirischen Nachweisen die fundamentalen Irrtümer auf, die der vorstehend geschilderten Annahme zugrunde liegen. Als Ergebnis zeigt sich, dass feindlichen Übernahmen bzw. Übernahmeveruche allenfalls eine marginale Bedeutung zukam. Das sollte eigentlich keine Überraschung sein, denn im Japan der Nachkriegszeit haben diese im Rahmen der Corporate Governance noch nie eine wesentliche Rolle gespielt.

Die Schlussfolgerungen, die sich aus diesem Beitrag ergeben, legen eine Zurückhaltung bei dem Versuch nahe, die Corporate Governance in Japan unter der Annahme einer zwangsläufigen Konvergenz mit dem US-amerikanischen Modell zu interpretieren. Die daraus abzuleitende Skepsis mag für andere Staaten hilfreich sein, die mit Blick auf die japanischen Erfahrungen versuchen, die Folgen der aktuellen Finanzkrise zu bewältigen.

(Dt. Übers. durch d. Red.)