1 Regulatory Background

1.1 Overview of Regulatory Background

There are six exchanges in Japan; Tokyo, Osaka, Nagoya, Sapporo, Fukuoka, and JASDAQ. Among these, the Tokyo Stock Exchange ("TSE") is by far the largest with 2,414 companies listed (including 25 foreign companies).

Stocks listed on the TSE are assigned to one of three markets: the First Section, Second Section, or Mothers (the market for high-growth and emerging stocks). Most newly-listed stocks begin on the Second Section with less strict requirements, and stocks for high growth, emerging companies are listed on the Mothers market. Currently, thirteen (13) foreign stocks are listed on the First Section and two (2) foreign stocks are listed on Mothers (as of May 31, 2010).

This chapter deals only with listing on the TSE.

First, the applicant company must meet the rules and guidelines of each exchange. The TSE checks the applicant company's conformity to the numerical criteria defined in the Criteria for Stock Listing Examination on an individual application basis, and conducts the examination with a focus on fair price formation and adequate distribution as well as the protection of investors and the public interest. Once all criteria have been satisfied, the TSE grants approval as a result of overall judgment. For complete details of the listing standards of the TSE, please refer to the Securities Listing Regulations at http://www.tse.or.jp/english.

Second, the process of the offer and sale of securities is subject to the Financial Instruments and Exchange Law (FIEL). The FIEL requires that each issuer who publicly offers securities in Japan disclose material information regarding its business and financial condition and the security being offered, by publicly filing a registration statement with the Financial Services Agency (FSA). Under the FIEL, issuers must provide a prospectus to potential investors. Issuers must also be prepared to meet the public company requirements of the regulations for management assessment and audit concerning internal control over financial reporting as a part of FIEL (J-SOX, the Japanese version of SOX). J-SOX requires the management of public companies to report annually on the effectiveness of internal control over financial reporting and management and to certify the completeness and accuracy of all disclosures in the company's FSA filings.

1.2 Regulatory Entities

The regulatory entities involved are the Financial Services Agency (FSA), a government organisation responsible for overseeing the financial industry.

1.3 Required Approvals
The TSE's approval is necessary.

2 Listing Criteria

Listing on the First and Second Sections

Applicant companies must satisfy the following numerical criteria before submitting an application for listing on the First or the Second Section. The criteria have been developed to ensure smooth circulation of shares and fair price formation, an applicant company's eligibility for listing in terms of corporate continuity, financial status and profitability, and appropriate disclosure of corporate information.¹

- Number of shareholders:
  - Second Section:
    - Single listing: 800 or more worldwide
    - Multiple listing: 800 or more in Japan
  - First Section:
    - Single listing: 2,200 or more worldwide
    - Multiple listing: 800 or more in Japan, and 2,200 or more worldwide.

- Tradable shares²:
  - Second Section:
    - Single listing: Applicant companies must meet the following requirements:
      a) Number of tradable shares: 4,000 trading units or more
      b) Market capitalisation of tradable shares: JPY 1 billion or more
      c) Ratio of tradable shares to listed shares: 30% or more
    - Multiple listing: No particular shareholder or holder of foreign stock depositary receipts, etc., holds an exceptionally large number of shares, and the number of tradable shares is 4,000 units or more.
  - First Section:

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² “Tradable shares” refers to listed shares excluding shares held by parties with a special interest such as officers, shares owned by the company itself, and shares held by persons who individually own 10% or more of listed shares.
Single listing: Applicant companies must meet the following requirements:

a) Number of tradable shares: 20,000 trading units or more

b) Market capitalisation of tradable shares: JPY 2 billion or more
   (transfer from the Second Section to the First Section, transfer from Mothers to the First Section shall apply.)

c) Ratio of tradable shares to listed shares: 35% or more

Multiple listing: No particular shareholder or holder of foreign stock depositary receipts, etc., holds an exceptionally large number of shares, and the number of tradable shares is 20,000 units or more.

- Market capitalisation of listed shares:
  - Second Section: JPY 2 billion or more
  - First Section: JPY 50 billion or more (JPY 4 billion or more for transfer from Mothers / Second Section to First Section).

- Number of years of business conduct: No less than three years under the board of directors.

- Shareholders' equity (consolidated): JPY 1 billion or more as of the end of the latest fiscal year before application.

- Amount of profit or total market capitalisation (whichever is smaller of the two: consolidated amount of current profit or consolidated amount of net income for the year before such adjustments as tax):

  - Applicant companies must meet one of the following requirements:
    - Profit for the most recent 2 years: (i) 1st year: minimum JPY 100 million, and (ii) 2nd year: minimum JPY 400 million;
    - Profit for the most recent 3 years: (i) 1st year: minimum JPY 100 million, (ii) 3rd year: minimum JPY 400, and (iii) total 3 years: minimum JPY 600 million; or
    - Total market capitalisation of minimum JPY 100 billion and sales of JPY 10 billion or more for the most recent year.

- False description, auditor's unfair opinion, etc.:
  - Second Section:
    - Fair opinion and no false descriptions for the last 2 years (or for the last 3 years if meeting the 3-year profit requirement)
■ Unqualified fair opinion for the latest year o First Section:

■ Same as for Second Section (in the case of transfer from Mothers / Second Section to First Section, fair opinions and no false descriptions for the last 5 years discovered).

■ Others:

  o Handlings of shares by Japan Securities Depository Center, Inc. (JASDEC), elimination of restrictions on transfer of shares must be agreed to.

  o For foreign depositary receipts, etc., conclusion of a depositary agreement.

Listing on Mothers

The following requirements relate to listing on Mothers. There are no criteria for financial performance such as profit, but Mothers-listed companies are required to publicise quarterly financial performance (a requirement since the market's opening that preceded the implementation of the same requirement for the First and Second Sections), and must hold corporate information sessions at least twice a year for the first three years following listing. These measures are part of the TSE's efforts to ensure market transparency.

- Eligible applicants: companies with high growth potential.

- Number of shareholders:

  o Single Listing: 300 shareholders worldwide  o Multiple Listing: 300 shareholders in Japan.

- Tradable shares:

  o Single listing: Applicant companies must meet the following requirements:
    a) Number of tradable shares: 2,000 trading units or more
    b) Market capitalisation of tradable shares: JPY 500 million or more
    c) Ratio of tradable shares to listed shares: 25% or more

  o Multiple listing: Number of tradable shares is 2,000 trading units or more.

- Public offering: 500 trading units or more.

- Market capitalisation: JPY 1 billion.
• Number of years of business conduct: No less than one year under the board of directors.

• False description, auditor's unfair opinion, etc.:
  o 2 terms (fair opinions and no false statements. Audit opinions must be "unqualified fair" for the latest term).

• Others:
  o Handlings of shares by Japan Securities Depository Center, Inc. (JASDEC), elimination of restrictions on transfer of shares must be agreed to.
  o For foreign depositary receipts, etc., conclusion of a depositary agreement.

2.1 Suitability / Eligibility of Listing Applicant

The listing examination covers the applicant company and its corporate group comprised of the applicant company, its subsidiaries, etc. The following items are examined and consideration is given to the legal systems, business practices, etc. of the applicant company's home country or the country in which the foreign stock exchange, etc. that lists or continuously trades the applicant company's shares is located.

First and Second Sections:

• Corporate continuity and profitability: The applicant company must conduct its business continuously and with a positive outlook for future business performance.

• Sound corporate management: The applicant company must conduct its business in a fair and honest manner.

• Effective corporate governance and internal control system: The applicant company must have built a proper framework for corporate governance and internal control.

• Appropriate disclosure of corporate profile: The applicant company must be capable of appropriately disclosing corporate information, etc.

• Other items that the TSE deems necessary in light of public interest and investor protection.

• Shareholders' rights and exercise of such rights are not unduly restricted.

• Relationship with a parent company and disclosure by such company are deemed appropriate.
• Other matters are deemed appropriate in light of the public interest and investor protection.

Mothers:

• Appropriate disclosure of corporate profile and risk information: The applicant company must be capable of appropriately disclosing corporate information, risk information, etc.

• Sound corporate management: The applicant is conducting its business in a fair and honest manner.

• Effective corporate governance and internal control system: The applicant company must have built a proper framework for corporate governance and internal control.

• Other items that the TSE deems necessary in light of public interest and investor protection.

• Shareholders' rights and exercise of such rights are not unduly restricted.

• Relationship with a parent company and disclosure by such company are deemed appropriate.

• Other matters are deemed appropriate in light of the public interest and investor protection.

• Shareholders' rights and exercise of such rights are not unduly restricted.

2.2 Track Record Requirement

The company must have been doing business for no less than 3 years under the board of directors.

A shorter track record is acceptable for listing on the Mothers market. The requirement is that the applicant's core business must be effectively operational for at least one year under a board of directors' control before the application date.

2.3 Eligibility for Electronic Settlement

The TSE uses an electronic, continuous auction system of trading. Brokers place orders online and when a buy and sell price match, the trade is automatically executed. All the securities must be handled by a designated central securities depository (Japan Securities Depository Center, JASDEC).

3 Overseas Companies

Foreign companies are eligible to list on the TSE, as can companies already listed on a foreign market.
The TSE's examination process for a foreign company's application takes approximately three months. Should listing approval be awarded, another month is required for equity finance. Therefore, an applicant company for listing should expect the process to take approximately four months between application and actual listing.

An applicant company can use the TSE's "preliminary consultation system" with a domestic securities company working as an intermediary to help identify and resolve potential difficulties in the examination before application.

The language of the documents must be Japanese (an English version can be attached).

An applicant company must furnish the TSE with a document showing that the decision for a listing application has been made by the board of directors.

For an initial listing of a foreign stock depository security, a copy of the document demonstrating that a depository agreement for the depository security for which a listing application is made must be supplied by the applicant company, as well as a copy of the document evidencing that the depository organisation of the depository security for which a listing application is made is in agreement on such matters as the TSE deems necessary.

4 Shareholding Requirements

4.1. Restrictions on Major Shareholders

When shareholders own more than 5% of the shares of a particular listed company, they must report to the FSA. Whenever their ownership ratio changes by more than 1%, a revised report must be submitted.

4.2. Post IPO Lock-up

For the First and Second Sections, the TSE imposes a mandatory six-month lock-up on shares issued during the fiscal year prior to the year of listing. Under this rule, conversion of preferred stock and exercise of options or warrants for common stock are each considered a new issuance to third parties.

There is no lock-up period on Mothers.

5 Listing Procedure and Timetable

12 to 24 months before admission:

- J-SOX compliance plan development.
- Corporate governance development.
- Engage lead underwriter.
4 to 12 months before admission:

- Begin to select other advisors, lawyer, etc.
- Prepare draft registration statement.
- Complete underwriter due diligence.
- "Preliminary consultation" with the TSE; initial meeting with stock exchange (TSE) and lead underwriter.

3 to 4 months before admission:

- Outside auditor review of draft registration statement.
- Audited financial statements prepared (audited semi-annual financial statements, if filing date is subsequent to nine months after current year end).
- Submit listing application to TSE.
- Start listing examination by TSE.

3 to 4 weeks before admission:

- Hearings from TSE.
- File initial registration statement with FSA.
- Accountant's comfort letter prepared and issued.
- Listing and stock exchange admission (pre-hearing period).
- Press release.
- Prospectus distributed.
- Roadshow presentations to prospective investors.
- Underwriter marketing of securities (bookbuilding).
- Offering declared effective by the FSA.
- Stock price approved by company Board of Directors Pricing Committee.
- Trading starts.

5.1 Marketing the Offer
The lead underwriter (a securities company) manages interactions with the financial community. It structures the offering, markets the securities to investors, develops pricing, and supports the offering in the initial period of trading.

5.2 Required Documentation

Documents to be lodged at the time of application are:

- Security Initial Listing Application Form (the name, class and number of shares, etc) with the Articles of Incorporation;
- "Written Oath Concerning Application for Initial Listing";
- Securities Report for Initial Listing Application (matters concerning the business group, status of its accounts, substance of the business, etc);
- Audit Report or Interim Audit Report prepared by at least two certified public accountants or an audit firm (excluding foreign companies);
- Audit Report or a document containing an opinion about financial values, etc. prepared by certified public accountants or an audit firm;
- calculation as specified by the Enforcement Regulations; and
- other documents specified in the Enforcement Regulations.

Documents to be lodged at the time of approval are:

- "Written Oath Pertaining to Timely Disclosure" and attached documents as specified by the Enforcement Regulations;
- the document stating to the effect that the representative of the initial listing applicant is aware that the "Securities Report for Initial Listing Application" the other documents specified by the Enforcement Regulations do not contain any untrue statements and the reason as specified by the Enforcement Regulations;
- the report containing matters concerning corporate governance specified by the Enforcement Regulations; and
- the report containing matters concerning risks of the business.

5.3 Publication of the Prospectus

After admission, the lead underwriter (a securities company) manages roadshow presentations to prospective investors and distributes the prospectus.

6 Documentary Requirements

6.1 Contents of the Main Listing Document
The content requirements include:

- information about the securities;
- information about the applicant;
- summary of the company, business, assets and facilities, conditions, accounting system;
- recent financial statements;
- shareholders;
- history of transfer of shares by interested parties;
- private placement;
- information about shareholders;
- profit and loss;
- business plan and perspective; and
- others.

6.2 Other Documents

A statement of legal opinion written by a legal professional certifying that matters pertaining to laws or regulations stated in the application for security listing and documents attached thereto are truthful and accurate must be provided by the applicant company. A document showing that a representative officer stated in the application for security listing is a person duly authorised to act for the listing of such security.

6.3 Articles / Constitutional Documents

Specific requirements are as follows:

- removal of restrictions on transfer of shares;
- official announcement to be made in daily newspapers;
- retention of a securities transfer agent;
- removal of bylaws that shorten notice period of shareholders' meeting;
- no accumulative votes for election of directors; and
- no restrictions on common stock preemptive rights.
7 Financial Information

7.1 Applicable Accounting Standards

As a general rule, the company to be listed is required to make its financial statements based on the accounting standards in accordance with the Business Accounting Council of Japan or Accounting Standards Board of Japan. However, the Japanese authority decides which accounting standards are to be applied to financial statements on a case-by-case basis for foreign companies. In past cases, the accounting standards of the applicant company's country of origin have been accepted for multiple listing. This may apply even to cases of single listing on the TSE when the applicant company has conducted appropriate disclosure of financial statements in its home country.

7.2 Period Covered by the Accounts

Either two or three years' accounts are required depending on whether the listing is on the First Section, Second Section or Mothers.

The five most recent fiscal years' consolidated financial statements are required to be submitted, if the company has made an annual securities report in the five most recent fiscal years.

7.3 Pro Forma Financial Information

The inclusion of pro forma financial information is allowed under the disclosure regulations.

7.4 Interim Financial Information

The company to be listed must submit its quarterly report for the first to third quarters of the most recent fiscal year.

8 Parties Involved

A company deals directly with the FSA, supported by its lead underwriter (a securities company), audit firm, and other advisors during the IPO process. The role of lead underwriter is very important throughout the IPO process in Japan.

The following are key Japanese parties who support the listing of foreign companies on the TSE. These participants work closely together during the preliminary listing process to support the preparation of the company for listing:

- Securities companies, which are TSE participants, provide professional advice and plan the schedule during the preparation phase. At the time of listing, they act as lead-underwriters of the issue.
• **Lawyers** examine legal issues during the preparation and application phase. After listing, the lawyer acts as the attorney-in-fact of the listed company, and undertakes activities such as corporate disclosure.

• **Audit firms** provide advice to applicant companies on their accounting systems and financial statements, and perform audits on the latter.

A sponsor must be a securities company and a participant of the TSE.

9 **Listing Costs**

9.1. **Listing Fees**

Foreign companies to be listed on the TSE must pay listing fees including, but not limited to, a listing examination fee, an initial listing fee, a public offering / sales fee, and an annual listing fee.

**Listing fees for First and Second Sections**

When the TSE is the main market:

• Listing examination fee: JPY 4 million.

• Initial listing fee:
  
  o JPY 15 million (First Section); o JPY 12 million (Second Section).

• Public offering / sales fee:
  
  o Number of offered shares x the offering price of new shares x 0.0009; o Number of existing shares offered x offering price x 0.0001.

• Annual listing fee:
  
  o JPY 0.96 to 4.56 million (First Section); o JPY 0.72 to 4.32 million (Second Section). When the TSE is not the main market:

• Listing examination fee: JPY 2 million;

• Initial listing fee: JPY 2.5 million (additional fees may apply);

• Public offering / sales fee: None;

• Annual listing fee: JPY 120,000 to 840,000.

**Listing Fees for Mothers**

When the TSE is the main market:

• Listing examination fee: JPY 2 million;
• Initial listing fee: JPY 1 million;
• Public offering / sales fee:
  o Number of offered shares x the offering price of new shares x 0.0009;
  o Number of existing shares offered x offering price x 0.0001;
• Annual listing fee: JPY 0.48 to 4.08 million (half for the first 3 years after listing).

When the TSE is not the main market:
• Listing examination fee: JPY 2 million;
• Initial listing fee: JPY 1 million;
• Public offering / sales fee: None;
• Annual listing fee: JPY 120,000 to 840,000 (half for the first 3 years after listing).

9.2. Sponsor's Fees

JPY 10 million or more (this depends on various factors).

9.3. Lawyers' and Accountant's Fees

JPY 10 million or more (this depends on various factors).

10 Corporate Governance Requirements

The company must follow corporate governance standards under the Japanese Companies Act and TSE requirements. Principal standards are as follows:

• board structure:
  o unitary (board of auditors required);
  o two-tier (optional);
• board composition is not specified;
• Audit Committee composition: majority of the auditors must be independent;
• remuneration disclosure is covered by Japanese disclosure rules.

The TSE announces principles of corporate governance as follows:
• corporate governance for listed companies should protect the rights of shareholders;

• corporate governance for listed companies should ensure the equitable treatment of all shareholders, including minority and foreign shareholders;

• corporate governance for listed companies should help create corporate value and jobs through the establishment of smooth relationships between the company and its stakeholders and encourage further sound management of the enterprise;

• corporate governance for listed companies should ensure that timely and accurate disclosure is conducted on all material matters including the financial condition, performance results and ownership distribution;

• corporate governance for listed companies should enhance the supervision of management by the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant groups, and ensure their accountability to shareholders.

11 Continuing Obligations

Tender Offer Rules under FIEL are applied when buyers purchase certain numbers of listed companies' shares by off-market trading.

12 Our Office

We can provide legal advice to foreign clients wishing to list on the TSE. For further information please contact Masahiro Nakatsukasa, (nakatsukasa_m@clo.gr.jp).

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