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A Study of the Current State and Problems of Japanese Restructuring

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Introduction

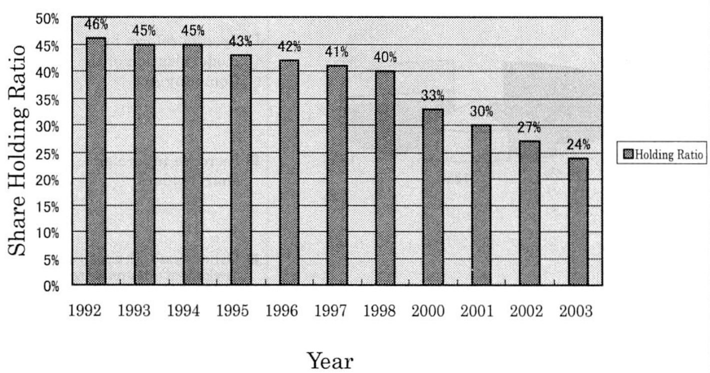
Evolution of restructuring of corporate organizations has been seen in various aspects combined with diversification strategy, internationalization strategy, and strategy for selection and concentration. In addition, it is deeply related to triangle accounting of the Financial Instruments and Exchange Act & the Company Act, the Tax Act and Accounting Standards. If one of them is deliberately ignored, contradiction in another place may arise. In this paper, I will therefore discuss issues which will be practical problems in evolving restructuring of corporate organizations.

1. Countermeasures for Hostile Takeovers

1.1 Surveys on the actual state for hostile takeovers

There are three types of hostile takeovers, which are green mails for the speculative purpose, M&As to expand business operation, and gaining profits in

Table 1. Stable Holding Ratio



trading in companies using investment funds.

In any case, a hostile takeover will be a major incident for a targeted company, and the company will take countermeasures. I will therefore look at surveys on the actual state of Japanese companies in relation to hostile takeovers[2].

Firstly, why do companies feel threatened by hostile takeovers? The reason originates from the fact that the shareholding ratios of main banks, which are stable shareholders, and other stable shareholder groups that include other banks, business customers, shares held by officers, employee stockownership schemes,

Table 2. How Companies Feel Threatened By Hostile Takeovers

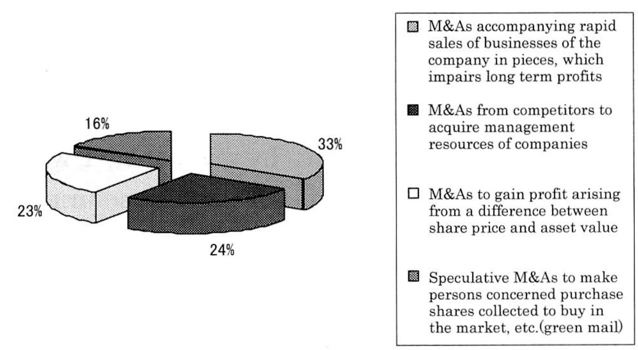


Table 3. Background for feeling threatened

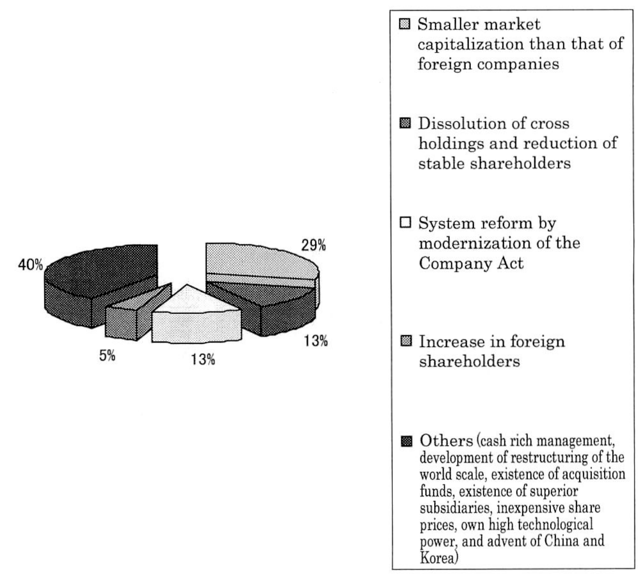


Table 4. Do share prices reflect corporate value?

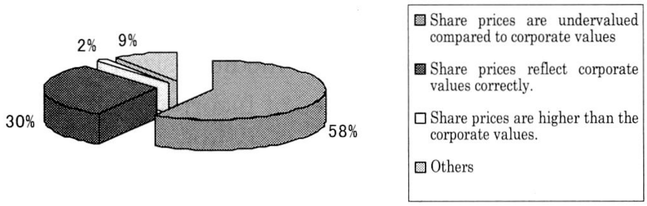
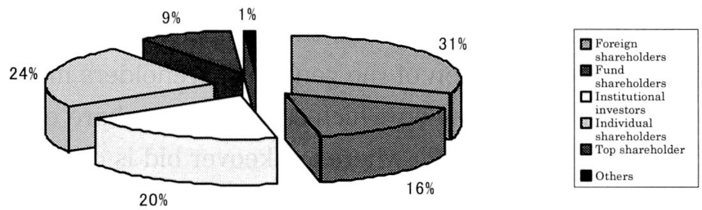


Table 5. Shareholders carefully looking at the trend



etc have become halved in the last ten years.

Secondly, there is a threat that one's own company will become the subject to sales in pieces as a general product. That depends on the increase or the size of the market capitalization of one' own company.

Thirdly, attention is paid to the trend of foreign shareholders and shareholders of funds who tend to become parties to hostile takeovers.

Fourthly, countermeasures for hostile takeovers will be created, and on the other hand, fair market rules will be required for an M&A. As a result, three principles, i.e., the principle of corporate value, security of common profits to shareholders and enhancement, the principle of prior disclosure and shareholders' intention, and the principle of the necessity and reasonability have been prescribed.[3)]

1.2 Usage of Class Shares

Under the Company Act, introduction of shares with a number of voting rights and shares with a veto (golden shares) have been permitted to prevent hostile takeovers, but the Tokyo Stock Exchange prohibits the introduction of these in principle[4)]. However, these class shares are the means which are effective for the corporate protection of unlisted small-and medium-sized companies.

For instance, Article 18 of the Articles of Incorporation of ITOEN listed on the first section of the Tokyo Stock Exchange reads "Where a company falls under each of the following items, on the day specified in each of such items (where the Board of Directors decide the date prior to that date, that date) the company shall acquire all of the class 1 preference shares remaining on that day, and the company shall deliver to the class 1 preference shareholders an ordinary share of the company per share of class 1 preference shares in exchange. (1) where a bill pertaining to a merger where the company becomes an extinguished company, and share exchange or share transfer (excluding share transfer made only by the company) where the company becomes a wholly owned subsidiary is approved by the general shareholders meetings of all the companies concerned (by the Board of Directors, where no resolution of the general shareholders meeting is required), on the day preceding to the day on which such merger, share exchange and share transfer become effective, and (2) where a takeover bid is carried out to the share certificates of ordinary shares of the company, and the ownership rate of share certificates, etc of a takeover bid (meaning as prescribed in Articles 27-2, Paragraph 8 of the Securities Exchange Act) exceeds 50%, on the 90th day from the day on which such ratio of ownership of the share certificates, etc. is recorded."[5)] This will have an effect as a countermeasure for a hostile takeover.

1.3 Equity Warrants

Firstly, a typical example of a countermeasure where equity warrants are used is the case of Bulldog Source[6)]. The decision of the shareholders on the necessity of discriminatory treatment of the acquisitor and its reasonability were considered important in the form of a special resolution in the general shareholders meeting. The necessity of a countermeasure for an acquisition where equity warrants are used can be made at the decision of management of the shareholders themselves, and it can be made either by an ordinary resolution or a special resolution. Reasonability of a countermeasure for an acquisition where equity warrants are used is evaluated in whether it is legally valued from the viewpoint of the principle of equity. To the shareholders other than an acquisitor, equity warrants and the shares are exchanged without money involved. However, to the acquisitor, equity warrants and the shares cannot be exchanged without money being involved, but equity warrants will be purchased at the TOB price. Money is compensated for to the acquisitor.

Secondly, there is a rights plan. This is a plan where equity warrants are issued to a trust bank, and where an acquisitor appears and a committee of third persons consider that it is a TOB, new shares will be allotted at favourable terms to the shareholders other than the acquisitor. There are three types of countermeasures for acquisitions where equity warrants are used. They are the class 1 type (rights plan with prior notice), the class 2 type (rights plan of a trust type) and the class 3 type (rights plan of a trust type and the SPC type). Shareholders other than acquisitors: equity warrants and shares are exchanged without money being involved, but transfer of equity warrants are not permitted to be made to acquisitors. In this case, this is usually not taxable for tax purposes, but is taxable in emergency defence cases[7].

2. Examination Items at the Time of Execution of Restructuring of Corporate Organizations

2.1 Existence of Agreements in Mergers

Close inspection (hereinafter referred to as "due diligence") is carried out concerning the state of the buyer, the company to be acquired, or the company which is a party to the merger in restructuring of an organization in accompaniment of an acquisition of a company, etc. In relation to due diligence, companies which are the parties to mergers under the item, representations and warranties, promise specific items with respect to the existence or non-existence of facts (for example, the accuracy of financial statements, non-existence of off-balance sheet debts, etc.) in detail, and where there is a breach of guarantee of the representations, it is said to be normal to have a clause covering compensation for compensation for damage, and this is to avoid risk to buyers[8].

I will therefore examine important points of due diligence, which are not often discussed.

Firstly, an important point is evaluation of change of control (capital control clause), that is whether or not examination has been carried out on the change of control whose structure such as immediate cancellation of license agreements, immediate repayment of loans, etc. at the time of the change of shareholders of a company and the change of the management is included. Change of control (capital control clause) has started as an item of countermeasures for hostile acquisitions. However, where the right of control which receives the provision of the license is exercised to carry out an M&A such as in a merger, share exchange, etc. and when another company and the company establish a merged company, the provider of the license may cancel the agreement or may require alterations to the agreement. The examples are the cases of Tanabe Seiyaku and Mitsubishi Pharma Corporation which merged on October 1, 2007. It has been reported that:– “from Centocore AG, which is a subsidiary of Johnson and Johnson, Tanabe Seiyaku acquired the right to develop and sell “Remicade” in Japan, which is a drug for articular rheumatism, and the company actually started to sell the drug in 2002, and is aiming to have annual sales of 50bn yen in 2010. After Tanabe Seiyaku and Mitsubishi Pharma Corporation merged to be called Tanabe Mitsubishi Seiyaku, the new company came under the umbrella of Mitsubishi Chemical Holdings and the right to control of Tanabe Seiyaku was changed. Tanabe Seiyaku has been emphasizing development, carrying out 5000 research after sales in the market. However, choices such as additional payment of licence fees, joint sales with Yansen Pharma in which J&J has an interest, negotiation of the capital control clause, etc. are assumed.”[9] However, Tanabe Mitsubishi Seiyaku after the merger was able to expand sales of Remicade by a large margin compared to the preceding term due to the effects of synergy of goodwill and improvement in efficacy helped by sustained R&D efforts. The company thus escaped from the negative action of this capital control clause.

Secondly, another important point is to examine whether or not evaluation of negative obligations arising from events that can be expected after the merger has been carried out in merger ratio computation. A typical example is provisions for damage guarantee as contingent liabilities.

Thirdly, the other important point is the issue of delisting criteria pertaining to loss of substantial continuity due to a merger by reverse acquisition, etc. In the case of Tanabe Mitsubishi Seiyaku, for example, as a result of a listed company (Tanabe Seiyaku) having merged an unlisted company (Mitsubishi Pharma Corporation) by absorption and substantial continuity of such listed company is not deemed to exist, listing will be cancelled and the company will become an unlisted company unless screening corresponding to initial listing is carried out within a certain period (within 3 years from the business year containing the year in which such a merger takes place) and the company passes the screening. Whether or not substantial continuity is lost will be questioned as a result of such listed company being affected by the execution of influential power of its parent company. On this point, Tanabe Mitsubishi Seiyaku has mentioned that the company is not affected by its parent company, Mitsubishi Chemical Holdings, in the following points. The statement reading "Mitsubishi Chemical Holdings (hereinafter referred to as "the parent company") is the parent company holding 56.46% of the voting rights of Tanabe Mitsubishi Seiyaku (hereinafter referred to as "the Company"), but there is no matter requiring prior approval of the parent company as to various decision matters in the execution of management. The core three companies held by Mitsubishi Chemical Holdings are the Company, Mitsubishi Chemical and Mitsubishi Resin and there is no competition between them. The main business of the Company is manufacture and sales of medical products for medical treatment, and certain independence from the parent company in capital relationship, where its business should be placed, human relations, etc." is represented by the Company.[10] As such a case, there was the case of Dainippon Sumitomo Seiyaku, but as a result of the screening, it was viewed as having substantial continuity. I consider that there will arise more issues concerning delisting criteria pertaining to loss of substantial continuity due to a merger by reverse acquisition, etc. in line with an increase in the number of merger cases in the future.

2.2 Impairment of Positive Goodwill

A matter that will be always required to be decided after a merger is impairment of goodwill and shares at the time of acquisition.

Firstly, an important point is that where impairment of goodwill is seen and the number of units of businesses acquired in transactions recognizing goodwill is more than two, the book value of goodwill will be split on the basis of reasonable criteria[11]. Because here is a synergy effect, etc. as to goodwill, impairment tests, a sign of impairment, and impairment loss can be measured in detail.

Secondly, another important point is impairment of securities after a merger. Daiichi Sankyo acquired Ranbaxy at 490bn yen in the preceding term, but an extraordinary loss of 402.6bn yen was accounted for in non-consolidated results due to a steep fall in the share price of the company. Because tax is not necessary to be accounted for due to this valuation loss being tax deductible as valuation loss of securities, this will be accounted for as deferred tax assets.

Deferred tax asset 242.6bn yen/Investment securities 402.6bn yen

Valuation loss of investment securities 160.0bn yen

This is based on the following provision concerning valuation loss of listed securities[12], reading "Concerning treatment of listed securities for long-term holding, in accounting for valuation loss of listed shares for tax purposes (impairment treatment for accounting purposes[13]), the share price has remained at 50% of the price corresponding to the book value for the last two years, and recovery of the share price is not expected in the near future". (Corporation Tax Act 33 2)) Verification of the possibility of recovery of the share price on valuation of investment securities is required. In this case, a reasonable decision is required to be achieved by carrying out analysis by individual stock and sector, etc. by professional securities analysts, and examination of the reasonability by an auditing firm in the process of audit is deemed to be the standard of inclusion in expenses[14].

Thirdly, where the interest of the acquiring company in net realizable assets acquired by a corporate combination by the purchase method, valued at a fair value, exceeds the acquired cost, the important points are recognition of intangible assets having a statutory useful life with respect to an amount corresponding to the excess, the standards of decisions at the time of composing goodwill and R&D expenses in progress, and accounting treatment of impairment and amortization of acquired goodwill after the merger. In several empirical researches into investment in R&D, capitalized value is permitted by investors as to investment in R&D which is amortized immediately for accounting purposes. There are some reports stating that share prices are formed on the basis that there are intangible assets[15]. The problems relating to these items will be clarified by carrying out management analysis of each item, and macro analysis is not suitable. I will not refer to this in this paper, as other papers have already clarified these.

2.3 Examination of Possibility of Restructuring of Organizations of Companies with Liabilities Exceeding Assets

Under the old Commercial Code, it was not permitted to make a company with liabilities exceeding assets a merged company. However, under the Company Act, it is a predominant view that a company with liabilities exceeding assets can be made a merged company.

Firstly, even if a company with liabilities exceeding assets is made a merged company, the state of liabilities exceeding assets will be resolved by carrying out evaluation of assets and liabilities at market value by the purchase method

Secondly, even if liabilities exceed assets in relation to the difference between assets and liabilities of a merged company after revaluation, it is still possible to offset the difference by accounting for goodwill.

Thirdly, a company with liabilities exceeding assets has been permitted to be a merged company, because it is possible to apply the provisions of the loss of a negative goodwill arising from a merger (the Company Act 795 2))[16].

Fourthly, where a company still remains a company with liabilities exceeding assets (a company with liabilities substantially exceeding assets) after revaluating assets, and if the principle of substantiation of assets is waived, it is understood that a merger can be made excluding cases where fulfillment of obligations cannot be estimated to be made after the merger[17].

Fifthly, share exchange and share transfer where a company with liabilities substantially exceeding assets is made a wholly-owned subsidiary are legally allowed as it is possible not to reduce assets of the company which wholly owns the subsidiary by reasonably setting the ratio of the share exchange and that or the share transfer[18].

2.4 Transfer of Business

Firstly, regarding the meaning of transfer of business, a special resolution at a general shareholders meeting is required to carry out transfer of all the businesses or part of an important business. However, regarding transfer of part of an important business, no resolution is required where the book value of assets does not exceed one fifth of the total assets (the Company Act, Article 467). There are three different views on this, which are as follows:–[19]

View 1 is that transfer of the business as prescribed in Article 467 is the same meaning as that in Article 21 of the Company Act and the provisions of the Commercial Code from Article 15. It is organized for business purposes and a transfer of the assets functioning as a tangible unity. In addition, it is accompanied by succession of business by an assignee, etc.

View 2 is that it is the transfer of assets for business purposes, and where it has a material effect on the destiny of a company which delivers the transfer, it will fall under transfer of the business. This is a view of a small number of people. A judicial precedent (the judgment of the supreme court on 22nd September 1965)

View 3 is that it must be the transfer of assets functioning as a tangible unity to make it fall under transfer of the business, but succession of the business is not required. In this case, human elements (customers, purchasers, labour force, etc.) must be transferred together. However, cases, where succession of purchasers is not allowed to take place but facilities of plants are transferred together with employees, will fall under transfer of the business. In addition, in transfer of the business as prescribed in Article 467 of the Company Act, there will naturally be a duty to avoid competition in Article 21 of the Company Act and Article 16 of the Commercial Code as in General Provisions.

Secondly, another important matter is reckoning the goodwill of a subsidiary company in the red. The capitalization method of excess earning power and the expected return method are usual methods in accountancy. However, in the case of a company which carries out transfer of the operations, in many cases operating profits and recurring profits are in the negative figures due to sales slump, and reckoning goodwill is therefore impossible by this method. Accordingly, the problem is whether or not there is goodwill in such a company in the red. According to a court precedent, where reckoning goodwill is not permitted, goodwill is the factual relationship that a company has intangible asset value which enables to generate corporate earnings exceeding those of other companies, that comprises long-term tradition and social trustworthiness, site location, existence of the special trading relationship, monopolistic nature of all these, etc., and it is therefore not appropriate to account for a value of goodwill because future excess earnings power is not deemed to exist."[20] In this sentence, excess earnings power is the element of judgement. On the other hand, there is a case where goodwill was permitted by evaluating the right of a sea course which was owned by a split company in the red. This case indicates that, without excess earning power, if there are legal goodwill, economic goodwill, human goodwill, site goodwill and latent assets, they will become elements of judgement On the side of a company which receives transfer of the operations, that will be acquisition for value of goodwill. However, the ground for computation must be required and, in addition, the acquisitor shall be responsible for proving the existence and the value of the goodwill[21]. For example, in cases of a company which receives transfer of the operations, the accumulating method where the value of goodwill is computed by taking the gross profit (for six months) of each store of its customers multiplied by the total number of the customers can be possible.

2.5 Examination of Takeover of Duties of Employees

Any of transfer of the operation (transfer of the business), company split and merger may be carried out as a means of corporate combination and corporate restructuring. However, unless the relation with the Labour Act is examined beforehand, hindrances may arise in management after restructuring of corporate organizations.

Firstly, in accompaniment of a company split, there was an incident which was disputed as to whether or not under an own labour agreement there was the right to refuse that transfer of duties of its employees should not be succeeded to a newly formed company. "According to the guidelines on taking appropriate measures concerning the succession of labour contracts and labour agreements where such split company has a tie up that should be taken by a split company, a newly formed company, etc., by the day on which the statement of the company split plan is placed within the headquarters of the company, the split company shall carry out negotiation as to whether or not labour agreements pertaining to such workers are to be succeeded, and the contents of the business where such workers are to provide services, the location where such service is to be carried out, and other forms of services, etc. in cases where such labour agreements are to be succeeded or in cases where such labour agreements are not to be succeeded respectively, after hearing individual persons' desires with full explanation to the workers who are engaged in the business that will be succeeded as to the summary of the company where such workers are to provide services after the company split and the way of whether or not such workers fall under workers who will be engaged mainly in the operations to be succeeded and other matters. (hereinafter referred to as "Article 5 Negotiation") and "A split company shall make efforts to obtain the understanding and cooperation of the workers that will be employed at all workplaces with labour unions, etc. organized by the majority of the workers at such workplaces, and the following subjects of the matters concerned are required, reading: 1) the backgrounds and reasons for the split of the company, 2) the estimated state of the fulfillment of the obligations for which the split company, the newly formed company, etc. are liable after the split of the company, 3) the standards for making decisions as to whether or not the workers fall under workers who are engaged mainly in the operations to be succeeded, 4) Matters concerning succession of labour contracts as prescribed in Article 6 of the Act on the Succession of Labour Contracts, and 5) proceedings for resolving problems for the purpose of the labour unions concerned which arise between a split company or a newly formed company at the time of the split of the company" (hereinafter referred to as "Article 7 Negotiation")[22].

Secondly, it is legally prescribed that the rights and duties of a company to be extinguished in a merger may be comprehensively succeeded to a surviving company or a newly established company. (The Company Act, Articles 750 1), 752 1), 754 1) and 756 1)). The labour contract matters of a company to be extinguished may be succeeded to a surviving company or a newly formed company. In addition, the labour contract matters may also be comprehensively succeeded in a company split.

Thirdly, the other important point is the relationship between transfer of the operations and the labour contract matters. I will examine below how transfer of takeover of duties of the employees should be dealt with in transfer of the operations where no provisions are prescribed as to the effects of comprehensive succession concerning this[23)]. It is whether or not labour contract matters may be prescribed as that labour contract matters cannot be transferred between the parties of transfer of the operations. There are a lot of cases stating as "Labour contract matters shall be naturally succeeded" to avoid excluding employees who do not follow the intention of the company at the time of transfer of the operations. On the other hand, where succession of labour contract matters are explicitly excluded between the parties of transfer of the operations, it is difficult to interpret that labour contract matters will be naturally succeeded. Another point is whether agreement of the workers is required, where labour contract matters are decided to be transferred between the parties of transfer of the operations (Civil Code. Article 625 1)). Transfer of the operations has been possible through the system to create the company split system since the amendment to the Commercial Code in 2000. Employment contracts have to be negotiated with workers, and labour contracts shall be succeeded. Where workers concerned state an objection to the succession of their labour contracts, those labour contracts shall not be succeeded.

2.6 Examination of Share Prices at the Time of Share Exchange

Share exchange is a method of corporate restructuring where the parent company owns 100% of the shares of a subsidiary company by issuing shares of the company which will become the parent company in exchange for the shares of its subsidiary from the shareholders of a company which is made to be the subsidiary company. In this share exchange, a listed company decides the ratio of share exchange on the basis of share prices. It is therefore possible to facilitate corporate acquisition by evolving share exchange at favourable terms.

Firstly, the Livedoor incident is an example. The Livedoor incident skillfully used a series of amendments to the Commercial Code (which eventually led to the establishment of the Company Act) which started in 1999. There were two classes of shares, par value shares (50 yen, 500 yen and 50,000 yen per share) and non-par value shares. However, par value shares were abolished and only non-par value shares became allowed to be issued at the time when amendments were made to the Commercial Code. In addition, under the Company Act expected to be enacted in 2006, there was a provision that a new joint stock company may be established with a paid-in capital of 1 yen. In this way, a share split had been prohibited where the net total assets amounted to less than 50,000 yen per share after the split before the amendments to the Commercial Code. However, the provision that the net assets per share (the total assets–the total liabilities) after a share split shall not be 50,000 yen or less was abolished and share split has become able to take place as many times as companies like, on the pretext that general investors will become able to buy shares more easily.

Livedoor started to carry out a split initially at the rate of 10 for 1 in August 2003 against the initial number of shares in issue being 10,000 shares, and continued to carry out a split at the rates of 100 for 1, 10 for 1 and 10 for 1 respectively, and as of the end of September 2005, the number of shares in issue rose to 1,049 million. As a result, the value per share normally falls, but it has risen because of the supply and demand situation, and the price earnings ratio which is an indicator of evaluation of financial results (meaning a ratio which is obtained by a share price based on a future estimated results divided by a profit per share) tends to be large in cases of small companies despite the share price being low. Incidentally, the price earnings ratio of Toyota Motors was 11.2x. The normal range was from 15x to 25x, but the price earnings ratio of the share price of Livedoor was abnomal, rising from 61.50x, 31.69x, 82.07x, 192.55x, and 496.67x. It may be criticized that this is a means to raise the share price and is excessive from the viewpoint of the protection of investors and the shape of the share price affected by this share split itself is deemed to be unreasonably raised, but this practice is legal under the Commercial Code.

Secondly, "the Toshi Jigyo Kumiai is a dummy fund of the Livedoor Finance, and the sale of shares of the Livedoor which was carried out under the name of the Kumiai is one substantially made by Livedoor Finance, and should be treated for accounting purposes as a sale of the shares of the parent company by a consolidated subsidiary. The sale proceeds must be accounted for as other capital reserves under Capital in its consolidated balance sheets, and is not allowed to be accounted for as sales in its Profit and Loss Statement."[24] Sale of treasury stocks is not a profit or loss transaction but a capital transaction. But the Livedoor concealed that, in the judgment of a lawsuit relating to compensation for damage, the Tokyo District Court ordered payment of 1,466 million yen concerning this case, acknowledging 200 yen per share as the amount of compensation for damage as a result of the sharp fall in the share price on the basis of the difference from the average share price for the period of a month before January 18, 2006 and a month after January 18, 2006 combined, on the date of which doubt of false statement of financial statements for the period ending September 2004 was reported by the Livedoor.[25]

3. Relation with Tax System

3.1 Issues Relating to Corporate Restructuring and Taxation

Firstly, an important point is matters relating to the organizational change of IRC. I will discuss restructuring strategies of corporate organizations from the tax viewpoint, under the tax system relating to restructuring of organizations in the USA in particular, by carrying out analysis of non-taxable combination transactions with respect to state income, tax matters in accompaniment of combination share transfer of foreign shareholders, and the relationship between deemed dividends by a spin-off of a subsidiary and foreign shareholders. In this case, the important matters relate to comparisons of the International Accounting Standards between Japan and the USA and the relationship between the tax system of restructuring of Japanese companies and the organizational change of IRC from the viewpoints of accounting and taxation. I will discuss accounting strategies of corporate combinations, under the tax system relating to restructuring of organizations in the USA in particular, by carrying out analysis of non-taxable combination transactions with respect to state income, tax matters in accompaniment of combination share transfer of foreign shareholders, the relationship between deemed dividends by a spin-off of a subsidiary and foreign shareholders.

Its typical example is deemed dividends by a spin-off of a subsidiary. Chugai Seiyaku carried out a spin-off by allotting capital reduction for value in the stock of Jane Broab Inc. (based in Santiago in the State of California, USA), which is Chugai Seiyaku's wholly-owned subsidiary of diagnostic drugs, to the shareholders of Chugai Seiyaku ahead of its share acquisition by Roche Pharm Holdings. The value of the shares of Jane Broab Inc. is 79.0bn yen (the book value at which Chugai Seiyaku acquired the stock was 25.6bn yen). As a result, tax withheld for deemed dividends amounting to 12,494 million yen was incurred, and corporation tax, habitation tax and business tax (after tax effects) pertaining to deemed profit on transfer amounted to 22,384 million yen[26)], and the result was that cash flow was substantially reduced due to the total tax charge amounting to approximately 35.0bn yen. Jane Broab Inc was later listed on the Nasdaq. This spin-off was carried out in accompaniment of a merger because of the violation of the anti-trust laws with respect to the market share in a specific field in the USA, and the Vice President of Chugai Seiyaku, Yuji Suzawa[27)], asserted, "It is impossible to carry out a bold business restructuring so long as such a rule exists." This raises tax issues also in cases where examination is required as to whether or not there is any violation against the anti-trust laws relating to the Fair Trade Commission in Japan.

Secondly, I will discuss problems relating to eligibility and non-eligibility under tax system in restructuring of corporate organization in Japan.

In cases where domestic companies transfer their assets due to restructuring corporate organizations, profit or loss on transfer of assets in cash transactions shall be accounted for in principle, and this is concerning whether or not it is taxable. However, profit or loss on transfer of old shares of the shareholders of the split company in a company split (the shares of a split company), and old shares of the shareholders of a merged company in a merger (shares of a merged company) shall be accounted for in principle. In these cases, tax to be charged shall be deferred as an eligible organizational restructuring from the viewpoint that there is no substantial economic change due to the continuity of investment in the shareholders' stage and the continuity of control of transfer assets in the corporation's stage.

In more detail, in an eligible organizational restructuring, the type of restructuring shall be either restructuring within a corporate group or a restructuring of a joint business, and an act shall start to be made practically after preparation to have the requirements for this.

Thirdly, the shares of a merging company used to be issued to the shareholders of a merged company. However, as a flexible measure for a merger consideration, shares of a parent company of a merging corporation became able to be issued to the shareholders of a merged company. This is called a triangle merger. Similarly, the number of triangle mergers, etc. is on the increase, wherein as a flexible measure for a consideration of a split, shares of a parent company of a split succession company may be issued and wherein as a flexible measure for a consideration of share exchange, shares of a parent company, which is a wholly-owning parent company of a share exchange may be issued. In these cases, such triangle mergers, etc. shall not fall under eligible mergers, etc. to prevent tax avoidance on the side of international tax charge, even if only the shares of a parent company are issued as a consideration of a merger, etc. where the shares of this parent company are the shares of a specified light tax charge foreign company to prevent tax avoidance on the side of international taxation.[28)]

Fourthly, concerning a tax matter where a share split, etc. by a merger with respect to tie-in shares, which are the shares of a merged company owned by the merging company immediately prior to a merger, a share split, etc. of these tie-in shares is deemed to have taken place (Article 61-2, 1) 2) of the Company Act), and profit or loss arises, and that will be taxable.

3.2 Losses Carried Forward and Tax Effect Accounting

Firstly, a loss carried forward of a consolidated company is offset by that of a consolidated tax payment group for that period, and will therefore be smaller than the figure of deferred tax assets accounted for in individual financial statements. For example, that is the reason why a figure of deferred tax assets accounted for in consolidated financial statements will become small in England where losses and profits are offset.

Secondly, where consolidated tax payment is made, recoverability of deferred tax assets shall be examined by the consolidated tax payment group as a whole with respect to losses carried forward of a parent company and a subsidiary company relating to the Corporation Tax Act. Recoverability is considered to be greater than that in individual statements in general.

In this connection, Hitachi Ltd. adopts consolidated tax payment, but the parent company, Hitachi Ltd. has announced that it intends to make listed subsidiaries wholly-owned subsidiaries (2009)[29], and prepared 200bn yen for a takeover bid.

This has double meaning.

Firstly, for accounting purposes, in consolidated accounts for the fiscal year of 2008, profits before minority interest amounted to 52,619 million yen, and the minority interest amounted to 110,744 million yen, which cannot be included in consolidated accounts.

	Ownership Ratio	Sales	Operating Profit
Hitachi Plant Technology	68.1%	¥359.6bn	¥7.3bn
Hitachi Maxell	51.4%	¥172.6bn	¥-2.3bn
Hitachi Information Systems	51.6%	¥192.0bn	¥11.6bn
Hitachi Software Engineering	51.3%	¥165.8bn	¥12.3bn
Hitachi System and Service	51.2%	¥126.2bn	¥7.3bn

Secondly, for consolidated payment, it was aimed to make subsidiaries wholly-owned subsidiaries, in order to solve the problem that losses of Hitachi Ltd. on a non-consolidated basis (i.e. as a parent company) cannot be deducted from profits of its subsidiaries, and that therefore valuation reserve, which means that losses cannot be carried forward as deferred tax assets, has to be accounted for. It can be seen that the balance of valuation reserve pertaining to deferred tax assets increased by 149,009 million yen as at end March 2008 and by 591,719 million yen as at the end of March 2009, respectivley.[30]

(Conclusion)

Research into corporate restructuring may be carried out using the method of macro analysis. However, I have taken up studies which included interesting issues for researchers and practitioners as parities themselves of restructuring participated and evolved due to change in the economic environment and the managerial environment, having different motives. By accumulating case study analyses, I consider that a lot of knowledge may be obtained with the environment and cases themselves as independent variables, restructuring motives of parties as parameters and restructuring acts as dependent variables.

This paper is the article shown in "Magazine" VOL. NO. (Moriyama Bookshop) with some addition and modification.

Notes

1) E-mail: cpayuokura@cosmos.ocn.ne.jp Ph. D. Certified Public Accountant in Japan.
2) The Ministry of Economy, Trade and Industry 'Survey on the actual state relating to hostile M&As of Japanese companies' "Guidelines on corporate value reports and policies concerning acquisition protection" A separate volume, Commercial Legal Affairs No.287.
3) "Guidelines on corporate value reports and policies concerning acquisition protection" (27th May, 2005).
4) The Tokyo Stock Exchange.
5) Provisions of the Articles of Incorporation of ITOEN concerning hostile takeovers (42nd ordinary general shareholders meeting on 26th July, 2007).
6) Bulldog Source Affairs.
7) Answers from the National Tax Agency dated 28th April 2005
8) Written with reference to 'Enterprise Acquisition and Opinion Guarantee Clause' prepared by Ryo Kobayashi in the "Separate Volume Jurist" to the Judicial Precedent Review No.341, Page 37 and NO. 194, Pages 50-51.
9) The Nikkei Sangyo Newspaper dated 28th March, 2007.
10) 'Matters concerning parent companies, etc." dated 19th June, 2009 from the home page of Tanabe Mitsubishi Seiyaku.
11) 'Application Guidelines on Accounting Standards Pertaining to Impairment of Fixed Assets" Details on Page 51.
12) National Tax Agency 'Q&A concerning valuation loss of listed securities' April, 2009.
13) Practical Guidelines Concerning Financial Products, Page 91.
14) National Tax Agency 'Q&A concerning valuation loss of listed securities' April, 2009.
15) "Advanced Accounting-Theories and Empirical Analysis-" by Takashi Ohinata, published by Chuokeizaisha in 2007, Page 91.
16) Ichiro Hara, 'Sorting-out and intensification of subsidiary companies, etc. and new establishment of joint holding companies', "Tax Affairs Case Study" Vol.107 (January 2009),

Page 10.

17) Shinsei Yonaga "Legal Mind Company Act, 11th version" published by Yuhikaku in 2007, Page 432.

18) Ibid, Page 433.

19) Tomotaka Fujita, 'Significance of Business Transfer-Judgement of Grand Bench of the Supreme Court on 22nd September 1965, 1961 (o) No.1357-' "Separate Volume Jurist" No.194, Pages 38-39.

20) Significance of Goodwill in Corporation Tax Act, 3rd July 1976 of the Supreme Court' "Judicial Precedent Review" No.831, Pages 29 to 30.

21) Sadao Maki, the chief of the Rulings and Legal Affairs Division of the National Tax Agency, 'Judgement on 27th March, 1976.

22) Judgement on 26th June 2008 of the Tokyo Supreme Court, "Judicial Precedent Review" No. 2026 dated 21st February 2009, Page 151.

23) Written with reference to 'Business Transfer and Labour Contract Matters" by Hiroshi Suzaki, Judgement on 26th March 1963 of the Osaka Supreme Court, "Separate Volume Jurist" Judicial Precedent Review No.341, Page 37, Ibid, No.194, pages 40-41.

24) Written with reference to the judgement of the Livedoor Incident Kose-appeal Hearing dated 25th July, 2008 referred to in "Judicial Precedent Review" No.2030, Pages 127 to 145.

25) The morning edition of the Nikkei Newspaper dated 10th July, 2009.

26) From "Financial Highlights for March 2003" of Chugai Seiyaku.

27) Yuji Suzawa, President of Chugai Seiyaku, 'Company Split and Hindrances to Business Reorganization', "The Nikkei Newspaper" dated 7th July, 2003.

28) Akio Nabeya (the Rulings and Legal Affairs Division of the First Taxation Department of the Tokyo National Tax Bureau, 'Reorganization Tax System' "Tax Study" No.695 (September 2007), Page 13.

29) The Nikkei Newspaper dated 27th July, 2009.

30) Securities Report of Hitachi Ltd. (from EDINET).