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Looking Through the Wrong End of the Telescope: The Japanese Judicial Response to Steel Partners, Murakami, and Horie

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LOOKING THROUGH THE WRONG END OF THE TELESCOPE: THE JAPANESE JUDICIAL RESPONSE TO STEEL PARTNERS, MURAKAMI, AND HORIE

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OVERVIEW: POISON PILL DOCTRINE IN SEARCH OF A PHILOSOPHY

When the *Bulldog Sauce* case[1] landed at the doorstep of the Japanese Supreme Court in July 2007, one suspects that the Court greeted it with all the enthusiasm of a homeowner who opens the front door to collect the morning paper, only to find waiting a basket full of orphaned kittens.

Unusually for a Japanese Supreme Court case, the *Bulldog Sauce* case attracted intense public scrutiny as an emblem of the struggle between a controversial new breed of corporate raider and the Japanese corporate establishment. But beyond that, in ways too subtle for headline news, the two lower courts arrived at the same destination through two entirely different paths of judicial reasoning, each of which presented its own set of awkward problems. The issues and the posture of the case were such that the Supreme Court could not easily resolve the split between the lower courts simply by endorsing one line of reasoning and rejecting the other.

How the Supreme Court resolved the *Bulldog Sauce* case, and the Japanese judicial response to the new breed of raider generally, reveals a great deal about the way the courts, and the Supreme Court in particular, think and function within the larger political and policy-making process. The inconsistent tangle of doctrines thrown up by the lower courts in the *Bulldog Sauce* case was the culmination of over two years of judicial efforts to accommodate defensive techniques against the new breed of corporate raider. The Japanese courts absorbed the consensus that *something* had to be done about the raiders and actively cooperated, judicially revising existing law and doctrine so as to overcome obstacles standing in the way of defensive techniques—in particular, poison pill—like stratagems. In doing so, however, they jumped straight from the premise that "something had to be done" to tinkering with specific

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1. Saikō Saibansho [Sup. Ct.] Aug. 7, 2007, 1809 JUNKAN SHŌJI HŌMU [SHŌJI HŌMU] 16.

statutory provisions that stood in the way, without pausing to factor in the real-world commercial context of different varieties of defensive techniques or the larger policies served by the legal "obstacles" they sought to overcome.

Examing legal problems through the wrong end of the telescope is not a phenomenon confined to the Japanese judiciary. It is endemic to Japanese legal education itself, which, unlike American legal education, focuses on mastering discrete statutes and rules in isolation and as given, rather than thinking about whether the rules make sense. It is reflected in a national landscape of rules mysteriously divided into a minefield of petty rules and regulations unimaginatively administered by officialdom, on the one hand, and another class of rules—such as those governing gambling, prostitution, and other underworld activities—that are conveniently ignored or evaded by painfully artificial fictions, on the other. The same root mentality is reflected in Japanese legal scholarship generally, which typically consists of low-to-the-ground summaries of existing law and scholarship without a transcending thesis. To take another field, Japanese politics in general are non-ideological and unprincipled, more defined by faction and relationships than principle or ideology. Socratic debate, principled argument and dissent, and elegant intellectual distinctions—this is not how Japan expresses itself.

As the judges in the *Bulldog Sauce* case experienced, interpreting and applying law low to the ground, case by case, without a broader policy perspective, is like cutting someone's hair up close without stepping back to survey the results. You cut the hair too short here, and too long there, and have to keep circling back to correct earlier miscuttings. The doctrinal twists and turns the law of poison pills has taken are largely attributable to the failure of Japanese courts to step back and address the issues more honestly and from a wider perspective.

The courts confronting defensive techniques thrown up to thwart the raiders viewed the problem as a narrow one, pegged to two specific provisions of the Company Law: (1) Article 247 of the Company Law,[2] which, as interpreted by a long and consistent line of precedent, prohibited management from issuing stock or stock rights to try to influence a control contest, and (2) Article 109 of the Company Law,[3] which codifies the

2. Article 247 of the Company Law provides that shareholders may demand that the issuance of rights to subscribe for new shares be suspended "when the issuance of the said rights to subscribe for new shares is to be conducted in a materially unfair manner." Kaisha-hō [Company Law], Law No. 86 of 2005, art. 247.

3. Article 109 of the Company Law provides that "[a] kabushiki kaisha (corporation) shall treat

long-standing case law principle that shareholders of the same class be treated on a nondiscriminatory basis. Poison pills and related defensive techniques that involve the issuance of stock or warrants on a discriminatory basis—as between the unwanted bidder and the remaining shareholders—bring directly into play both of these statutory provisions, as well as the policies which presumably lie behind them.

From the beginning, the Japanese courts focused narrowly on Article 109 and Article 247, each viewed as a separate and discrete problem, and sought to fashion new doctrines built around the statutory provisions that would accommodate what they understood to be the "Japanese poison pill." The issue was defined at the threshold as one involving the legality of a "discriminatory issuance of warrants." So framed, the courts could see no relevant distinction between a typical poison pill, designed to give management leverage to negotiate better terms with a bidder, and the Bulldog Sauce warrants, which had the entirely different effect of forcing Steel Partners to cash out shares it already owned and expelling it as a shareholder. Since both took the form of a "discriminatory issuance of warrants," they were treated as indistinguishable. Similarly, because the problems were analyzed through the narrow prism of discrete statutes, rather than broader policies, the courts had no answer to the legality of other defensive techniques that did not involve the issuance of stock rights or were not overtly "discriminatory." Lacking a philosophy or a policy framework to analyze defensive techniques in corporate control contests, the courts were like the blind men stroking the trunk, ears, and other appendages of the elephant.

One might infer that the Supreme Court felt that the new (and inconsistent) corporate law doctrines declared by the two lower courts were not only extreme in a substantive corporate law sense, but that the herky-jerky judicial process that generated the doctrines was itself suspect. By the time the case reached the Supreme Court, it was too late to unscramble and relitigate the issues. The Supreme Court accepted the categories it inherited from the lower courts, but manipulated the same abstract doctrines and verbal formulas in a way that essentially declawed the decision. Thanks to the Supreme Court's deft surgery, as a corporate law decision, and in particular a guiding precedent on the Japanese poison pill, *Bulldog Sauce* ends not with a bang, but a whimper. If it has anything

its shareholders equally in accordance with the particulars and number of shares held by them." *Id.* at 109.

to say, it is limited to the exceptional facts of the *Bulldog Sauce* case itself, which are unlikely to recur.

The *Bulldog Sauce* case itself ended harmlessly, if not pointlessly, but as I will argue in the final section of this essay, the judicial mentality that drove its decision is not always harmless. Judicial accommodation of prevailing consensus is harmless so long as the consensus it reflects is benign. But, as the collective overreaction to the new breed of raiders shows, the shifting tides of consensus can take the form of a collective rush to judgment against which courts should serve as an autonomous check. The Japanese courts uncritically accepted the prevailing official consensus that the new breed of raider was a malignant influence. The courts were shamefully complicit with the national prosecutors in applying the criminal laws without a full comprehension of the relevant commercial context to convict Yoshiaki Murakami and Takafumi Horie, the highest-profile domestic raiders, and put them out of business. In a criminal context, the courts applied rules mechanically without pausing to think or explain what was offensively criminal about what the defendants actually did or who had actually been harmed.

A. Article 247: Misdigested Delaware Jurisprudence

1. Legal Obstacle to the Poison Pill

Article 247 of the Company Law authorizes injunctions against the issuance of stock warrants "when the issuance of the warrants is to be conducted in a materially unfair manner."[4] By its terms, Article 247 applies to the issuance of stock rights and not other forms of transactions that could be used to impede a bid for control. A fairly consistent line of cases, as well as the accepted academic view, has held that the issuance of stock rights, the "primary purpose" of which was to influence or impede a bid for control, was "materially unfair" and therefore enjoinable.[5] Article 247 had been successfully invoked when management of target companies tried to block a change of control to an unwanted bidder by issuing share

4. *Id.* art. 247, para. 2.

5. See discussion of precedents in Y. Ota & S. Noda, *Kigyo bashu boeisaku to shite no dai-san wariate zoshi to sono mondaiten* [*Issues Involved in the Use of Stock Issuance to Third Parties as a Takeover Defense*], *in* TEKITAITEKI M&A TAIŌ NO SAISENTAN [Leading Edge Techniques in Hostile M&A] 169–75 (Y. Ota & R. Nakayama eds., 2005); KENJIRŌ EGASHIRA, KABUSHIKI KAISHA HŌ [CORPORATION LAW] 682–83 (2005), and academic articles cited therein.

rights to a friendly third party—the method Japanese companies have typically used to defend themselves against unsolicited bids.[6]

The policy behind this case law, though not elaborately spelled out in the cases, was fairly straightforward. Management should stay out of voluntary transfers of shares between and among shareholders. Shareholders are competent to look out for themselves. The securities markets generally work efficiently, and changes in control generally promote economic efficiency. Management's motives for wanting to block a bid are suspect to the extent that they stand to lose their jobs if a change in control does take place.

These policy assumptions reflect liberal, free-market ideas about shareholder competence, market efficiency, and the risks of management self-dealing. It is consistent with the basic policy assumptions, for example, of Delaware corporation law and Delaware jurisprudence relating to corporate control contests.[7]

The Japanese establishment's interest in Article 247 and mergers and acquisitions (M&A) law more generally began in 2000 when Yoshiaki Murakami, a former Ministry of Economy, Trade, and Industry (METI) official, launched the first postwar hostile tender offer against Shoei, a little-known real estate and electronic parts company.[8] Alarm within corporate Japan accelerated in late 2003, when Steel Partners made hostile bids against two other small companies, Yushiro and Sotoh, and gained further momentum in 2004 when Murakami initiated a control contest for Nippon Broadcasting System (NBS).[9] The panic peaked in 2005 when Takafumi Horie announced he had secretly acquired (mostly from Murakami, it turned out) a large block of NBS shares and was launching a tender offer.[10]

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6. *See, e.g.*, Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] July 25, 1989, 704 HANREI TAIMUZU [HANTA] 84. As a recent and well-publicized example, in 2006 Hokuetsu Paper Mills warded off a hostile bid by Oji Paper by issuing shares to "friendly" Mitsubishi Corporation and Nippon Paper. Yasuyuki Onishi, *Oji Paper Encounters Unexpected Difficulties in Hokuetsu Takeover Bid*, NIKKEI BUS., Aug. 21, 2006, *available at* http://business.nikkeibp.co.jp/article/eng/20061206/115010/.

7. *See* Richard E. Kihlstrom & Michael L. Wachter, *Corporate Policy and the Coherence of Delaware Takeover Law*, 152 U. PA. L. REV. 523 (2003).

8. See ENRICO COLCERA, THE MARKET FOR CORPORATE CONTROL OF JAPAN 110 (2007) for an account of Murakami's campaign against Shoei.

9. *Id*. at 111–12.

10. For a journalistic account of Murakami's and Livedoor's actions in relation to NBS, see YASUAKI ŌSHOKA, HIRUZU MOKUJIROKU: KENSHŌ RAIBUDOA [HILLS APOCALYPSE: LIVEDOOR UNDER INVESTIGATION] (Asahi Shimbun-sha, 2006).

2. *The Kanda Committee's Blueprint for the Japanese Poison Pill*

Article 247, as it had been interpreted by the courts, posed a problem because it did not provide for any exceptions. Under existing precedent, if there was an issuance of stock rights and the "primary purpose" was to block a hostile bid, it was legally dead. Unless this obstacle could be somehow dealt with, the Japanese poison pill was also dead. To address the problem, in September 2004, METI announced the formation of an informal Corporate Value Study Group[11]—headed by Professor Hideki Kanda of Tokyo University, manned by prominent foreign-trained Japanese corporate lawyers from the large Japanese firms and legal academics, and "advised" by Sullivan & Cromwell and Lazard Freres—to "study" the feasibility of adopting an American-style poison pill within the Japanese legal and regulatory framework. It seems clear that the committee's mission was to study not whether, but how, to facilitate the poison pill in a Japanese context.[12]

Awkwardly, the Kanda Committee issued its report in May 2005, just two months before the new Company Law was promulgated. The report acknowledged that Japanese law surrounding corporate control transactions is highly unsettled and that "rules" (presumably legislation) needed to be urgently promulgated to ensure that the defensive arrangements adopted by Japanese companies are neither overly nor insufficiently protective.[13] The committee implicitly recognized its own lack of legal authority to create rules and beckoned the legislature to do so. Yet, two months later, the new Company Law was promulgated without any mention of poison pills or other defensive arrangements.

The Kanda Committee surveyed foreign law and precedents, both American and European, to serve as possible models and reference points for the Japanese poison pill. This type of multijurisdictional survey is the time-honored practice of ministry-appointed committees charged with proposing new policy or legislation.[14] The model that the study group presented as the best one for Japan to emulate was Delaware's model, in

11. CORPORATE VALUE STUDY GROUP, CORPORATE VALUE REPORT (May 27, 2005), *available at* http://www.meti.go.jp/policy/economic_oganization/pdf/houkokusyo_hontai_eng.pdf [hereinafter CORPORATE VALUE REPORT].

12. The Kanda Committee was convened under the auspices of METI's Policy Division, headed between 2004 and 2006 by Takao Kitabata. Kitabata subsequently attained notoriety as Vice Minister from 2006 to 2008 for his colorful theory of "good" and "bad" shareholders and for taking frequent potshots at Steel Partners and other foreign "activist" funds.

13. Corporate Value Report, *supra* note 11, at 112.

14. Multi-jurisdictional surveys are also a dominant format of Japanese legal scholarship.

particular the framework of analysis established in the *Unocal* case.[15] The report characterized Delaware law and the Unocal case at a very high level of abstraction. It reported that Delaware permitted defensive measures that met the following criteria and recommended that Japanese law follow suit:

> (i) whether there are reasonable grounds to believe that there is a threat to corporate value when a defensive measure is triggered; (ii) whether a defensive measure to eliminate the threat is excessive; and (iii) whether the board has made a prudent and independent decision on the reasonableness of a defensive measure.[16]

At this high level of generality, the criteria become virtually meaningless and fail to convey the richness and complexity of the law of control transactions in Delaware under *Unocal* and its many progeny. Delaware M&A jurisprudence embodies a theory of dynamic relationships between and among management, controlling shareholders and minority shareholders as well as the courts.[17] The underlying theory is expressed doctrinally in terms of the "business judgment rule"—a series of boundary-setting conditions that differentiate between management actions (including defensive techniques) that the courts will not second guess because the shareholders are presumably adequately protected and others that call for special scrutiny by the courts.[18]

At the outset, one of the fundamental conditions required by *Unocal* and other Delaware cases in order to insulate a management decision from judicial second guessing is that the decision be approved by a majority of independent outside directors. If this condition is met, suspicion that management self-dealing is at play abates.[19] The Kanda Committee report, however, conveniently glossed over this requirement, presumably because of the fact that the overwhelming majority of Japanese public companies do not have meaningful numbers of independent outside directors.[20] At the threshold, one of the basic predicates for importing *Unocal* into Japan was missing.

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15. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).

16. Corporate Value Report, *supra* note 11, at 85.

17. *See supra* note 7.

18. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 90 (1991).

19. *Unocal*, 493 A.2d at 955.

20. Companies listed on the Tōkyō Stock Exchange have an average of 0.86 "outside" directors. TŌKYŌ STOCK EXCHANGE, TSE-LISTED COMPANIES: WHITE PAPER ON CORPORATE GOVERNANCE 19 (2009), *available at* http://www.tse.or.jp/english/rules/cg/white_paper09.pdf.

In any event, a written summary, no matter how detailed, could not provide a realistic substitute for the nuances and architecture of a jurisprudence that developed organically in Delaware over several decades. To give abstract criteria distilled from Delaware jurisprudence to Japanese courts and to expect the courts to use those criteria to generate coherent results is like telling someone golf is about using a stick to put the ball in the cup in as few strokes as possible and expecting them to use the information actually to play golf.[21]

3. *Livedoor-NBS's Delaware-Inspired Dicta*

In Spring 2005, just as the Kanda Committee was putting the finishing touches on its report, the picture was further complicated by Takafumi Horie's announcement that his company, Livedoor, had covertly acquired thirty-five percent of NBS shares and was launching a tender offer to take control of NBS.[22] This captured headlines across Japan and prompted NBS and its affiliated large shareholder, Fuji Television, to resort to a crude but common defensive tactic in Japan (not to be confused with a poison pill): NBS issued a large slug of warrants to Fuji Television that, when exercised, would cause Livedoor's shares to be diluted.[23]

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21. The differences in the way Japanese courts and Delaware courts approach corporate law problems is illustrated by two M&A cases decided at roughly the same time. Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914 (Del. 2003) involved the enforceability of a merger agreement after a new bidder arrived before the closing to offer more attractive terms. A closely divided Delaware Supreme Court held that management of the target company had a fiduciary duty to their shareholders to entertain higher bids even after a merger agreement had been signed and that shareholder interests would be best served by allowing the higher bid to win. *Id*. at 918. The validity of the merger agreement was viewed in *corporate* terms, i.e., the interests of shareholders as intermediated by their fiduciary agents, by the board of directors. By contrast, in Sumitomo Trust v. UFJ Holdings, Saikō Saibansho [Sup. Ct.] Aug. 30, 2004, 1708 SHŌJI HŌMU 22, the Japanese courts were called on to enforce an agreement in which the parties agreed to negotiate exclusively with each other regarding a possible merger. The exclusive negotiating agreement became an issue when, as in *Omnicare*, a third party arrived to offer better terms. The Japanese courts upheld the enforceability of the exclusive negotiating contract, which they viewed as a simple contract law issue that had no relation to possible shareholder interests. *Id*. at 24–25; *see* Hiroyuki Tezuka, *M&A keiyaku ni okeru dokusenken fuyō to sono genkai* [*Exclusive Negotiating Rights in M&A Agreements and Their Limits*], 1708 SHŌJI HŌMU 12 (2004) (arguing that the courts in *Sumitomo Trust-UFJ Holdings* did not give sufficient attention to the corporate dimensions of the exclusive negotiation agreement).

22. *Nippon hoso kabu—Raibudoa ga 35% shutoku* [*Livedoor Acquires 35% of Livedoor*], YOMIURI SHIMBUN, Feb. 8, 2005, *available at* http://www.yomiuri.co.jp/atmoney/mnews/20050208mh12.htm.

23. *Arata na boei shudan? Shinkabu yoyakuken* [*A New Defensive Technique? Warrants to Acquire Newly Issued Shares*], YOMIURI SHIMBUN, Feb. 25, 2005, *available at* http://www.yomiuri.co.jp/atmoney/mnews/20050225mh12.htm.

Livedoor filed a lawsuit in the Tokyo District Court to enjoin the warrants under Article 247.[24] This presented the Tokyo District Court with a hot potato. The factual background indicated clearly that the sole purpose of the warrants was to block Livedoor. Therefore, the court was pushed firmly by precedent to issue an injunction.[25] On the other hand, it was widely known that the Kanda Committee was at work establishing a legal framework for the Japanese version of the poison pill—and a poison pill, after all, is an issuance of warrants designed to block a bidder's attempt to gain control.[26] The cross currents can be sensed in the Livedoor-NBS opinions—the push of settled precedent against the pull of an imminently expected, but still unformed and unpublished, proposal to amend the law.

The Tokyo High Court's decision was issued in March 2005, two months before the official publication of the Kanda Committee report.[27] The inference seems strong that the courts, METI, and the Kanda Committee were in direct or indirect communication with each other.[28] The Tokyo High Court, based on the weight of existing precedents, enjoined the warrants. At the same time, however, the court issued remarkably detailed dicta, almost certainly based on intelligence supplied by METI and the Kanda Committee about Unocal and Delaware law, which spelled out the kind of "abusive" bidder it *would* be legitimate to try to obstruct:

> (1) the case where the acquirer accumulates the target shares for the purpose of making the concerned parties of the company buy back the shares at a higher price by driving up share prices, though there exists no true intention of participating in management of the company (the case of the so-called "greenmailer");
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> (2) the case where the acquirer accumulates the target shares for the purpose of an abusive acquisition, such as temporarily taking control of management of the company and transferring assets

24. Livedoor v. Nippon Broad. Sys., Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] Mar. 11, 2005, 1173 HANREI TAIMUZU [HANTA] 140.

25. *Id.* at 149.

26. Ministry of Economy, Trade and Industry, http://www.meti.go.jp/policy/economy/keiei_innovation/keizaihousei/ma_rule.html (last visited May 7, 2011).

27. Livedoor v. Nippon Broad. Sys., Tōkyō Kōtō Saibansho [Tōkyō High Ct.] Mar. 16, 2005, 1173 HANREI TAIMUZU [HANTA] 125.

28. Needless to say, it would be viewed as inappropriate in most jurisdictions for an administrative agency to communicate ex parte with a court concerning a pending case. MODEL CODE OF JUDICIAL CONDUCT Canon 3.B(7) (2004).

necessary for business operations of the target, such as intellectual property, know-how, confidential business information, and information as for major clients and customers, to the said acquirer or its group companies;

(3) the case where the acquirer accumulates the target shares in order to pledge the target's assets as collateral for debts of the acquirer or its group companies or as funds for repaying such debts, after taking control of the company;

(4) the case where the acquirer accumulates the target shares for the purpose of temporarily taking control of management of the company so as to dispose of high-value assets such as real estate and negotiable securities that are currently not related to the company's businesses and pay temporarily high dividends out of proceeds from the disposition, or sell the shares at a higher price because share prices have risen rapidly due to temporarily high dividends.[29]

The first category, "greenmail," had been mentioned in *Unocal* as a "threat" against which a board could legitimately try to protect the corporation and was also referred to as a legitimate "threat" in the Kanda Committee report.[30] The second category, corporate "looting" or "scorched earth" tactics, though not specifically mentioned in the Kanda Committee's report, was treated in some Delaware cases as a "threat" against which management would be justified to take action.[31] The third and fourth categories—leveraged buyout acquirers and bust-up acquirers—have never been characterized as "threats" justifying defensive measures in Delaware law and were not mentioned in the Corporate Value Report. But the inclusion of this type of perceived short-term, financially motivated acquirer (as opposed to long-term, strategically motivated acquirer) as "abusive" was quite consistent with "bad" shareholder theory being developed within METI's Policy Division, the Kanda Committee's sponsor. The third and fourth categories, in particular the fourth category, seem to be designed to capture bidders like Steel Partners.[32]

29. *Livedoor*, 1173 HANREI TAIMUZU [HANTA] at 133.
30. Corporate Value Report, *supra* note 11, at 87.
31. *See, e.g.*, Cheff v. Mathes, 199 A.2d 548 (Del. 1964).
32. When the Kanda Committee report was published two months later in May 2005, it recycled the dicta in *Livedoor* as legal authority for its proposed list of "threats" that justify defensive measures. *See* Corporate Value Report, *supra* note 11, at 23.

Normally, issuing unnecessary dicta, especially at this level of detail, would be considered poor judicial practice.[33] So would a court's accepting of ex parte coaching on legal issues involved in a pending case from an administrative agency. But more than this, what one looks for in vain in the *Livedoor* decisions is a coherent explanation of the policy underlying the four categories. The four categories are in part, it is clear, somehow derived from Delaware law. But the larger framework and methodology used by Delaware courts is completely missing. Delaware M&A jurisprudence is not a set of cookie-cutter formulas and answers; it is a finely structured way of thinking about a set of issues. Why, as Article 247 precedents tell us, should management "in principle" not interfere with contests among shareholders for corporate control? Why is this pegged as an Article 247 issue—that is, one that relates specifically to the issuance of warrants—rather than a broader one linked to something like the business judgment rule? What are the exceptions to the general rule, and what is their justification? Why, for example, do leveraged buyouts pose a threat? What is wrong with selective sale of a target company's assets? On these questions, the decision is a total blank. The four categories were simply delivered cold, from the hip, without explanation or context.

The report of an unofficial study group and dicta in one opinion are fairly shaky legal ground, but corporate Japan took them as a green light for the Japanese poison pill. Lazard Freres and Sullivan & Cromwell, the foreign investment bank and law firm that had provided the Kanda Committee with intelligence about Delaware law and American M&A practice, put their credentials to work and advised Nippon Steel and others on the implementation of formidable poison pills.[34] In the three years following the Kanda Committee report, over five hundred Japanese companies adopted poison pills patterned on the blueprint provided by the study group.[35] The kittens were now out of the bag.

33. Felix Frankfurter, *A Note on Advisory Opinions*, 37 HARV. L. REV. 1002 (1924).

34. Press Release, Nippon Steel Corp., Nippon Steel Announces the Adoption of Fair Rules for the Acquisition of Substantial Shareholdings (Takeover Defense Measure) and the Shelf Registration of Stock Acquisition Rights (Mar. 29, 2006), *available at* http://www.nsc.co.jp/data/200603301151 30.pdf.

35. Corporate Value Study Group, Takeover Defense Measures in Light of Recent Environmental Changes 3 (2008), *available at* http://www.meti.go.jp/english/report/data/080630Take overDefenseMeasures.pdf.

4. *Bulldog Sauce: The Poison Pill that Wasn't*

This was essentially the state of Article 247 jurisprudence when Steel Partners made an unsolicited bid for Bulldog Sauce, offering the company's shareholders a twenty-five percent premium over the prevailing market price. It is not clear whether the courts fully appreciated it, but the Bulldog Sauce plan that was adopted to fight off Steel Partners was not really a poison pill at all. True, on the surface, both the Bulldog Sauce plan and a poison pill involve the issuance of stock rights in a manner that discriminates against the bidder. But there the differences begin.

A poison pill is typically adopted before a specific bidder appears on the scene and gives management a lethal weapon—the ability to issue warrants that will dilute and destroy the economic value of the bidder's stock—if the bidder acquires more than a given threshold percentage (typically twenty percent) of the company's stock.[36] The poison pill gives management the ability to point a gun and say, "Cross this line and we will shoot. Now let's have a discussion about your price." A poison pill is not meant to block takeovers, it is meant to give management leverage and time to negotiate "fair" terms on behalf of shareholders.[37] Poison pills are almost never actually triggered because it would be suicidal for the bidder to cross the line and invite being shot.

The Bulldog Sauce rights plan, by contrast, was adopted by shareholders (83.8% of them) and *actually triggered after* Steel Partners appeared on the scene and launched a tender offer.[38] Moreover, the warrants in question were not a lethal weapon designed to destroy the economic value of Steel Partners' stock if it crossed a line, but in effect compelled Steel Partners to cash out and sell three-quarters of stock it *already* owned back to the company at the market price. The point of the Bulldog Sauce plan was not to keep Steel Partners at bay and enable management to negotiate a better deal, but coercively to buy out and expel Steel Partners as a shareholder.[39] The warrants were just an incidental formal detail.

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36. Alessandro Presti, *Poison Pills: Too Strong or Just Right?*, COLUM. BUS. L. REV. ONLINE (2011), *available at* http://cblr.columbia.edu/archives/11580.

37. Ronald J. Gilson, Unocal *Fifteen Years Later (And What We Can Do About It)*, 26 DEL. J. CORP. L. 491 (2001); Martin Lipton & Paul K. Rowe, *Pills, Polls and Professors: A Reply to Professor Gilson*, 27 DEL. J. CORP. L. 1 (2002); Ronald J. Gilson, *Lipton and Rowe's Apologia for Delaware: A Short Reply*, 27 DEL. J. CORP. L. 37 (2002).

38. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] June 28, 2007, 1805 SHŌJI HŌMU 43, 46–48.

39. Technically, the plan worked as follows: All shareholders would be issued warrants

Another dimension that the courts did notice, but the implications of which they did not fully comprehend, was that 83.8% of the shareholders—essentially all shareholders other than Steel Partners itself—had voted in favor of a cash-out that would expel Steel Partners as a shareholder and, with it, destroy any chance they might have to induce Steel Partners to offer an even higher premium.[40] What the Bulldog Sauce shareholders were saying was that they did not want Steel Partners' money, period—no matter how much they were offered. The shareholders did not adopt the "poison pill" because they thought the premium being offered was inadequate and wanted to ratchet up the price. They were saying that they did not want Steel Partners to buy their shares *at any price*.[41]

5. *The District Court's Midflight Correction and the High Court's Hijack*

These were the facts which the Tokyo District Court put through the mill of Article 247. In light of the dicta in the *Livedoor* case, the most straightforward way of resolving whether the Bulldog Sauce warrants were "materially unfair" would have been to find that Steel Partners fit under one of the four "abusive acquirer" categories. But the district court, perhaps feeling that the evidence did not support such a finding, or in any event that such a finding would be controversial, tried to finesse the issue by creating yet another gloss on the "abusive acquirer" doctrine. The court held, in the form of a new evidentiary rule, that if a majority of shareholders vote to take defensive measures against an identified bidder, the bidder is presumptively an "abusive acquirer."[42] Therefore, the district court concluded that it was "not necessary" for it to make its own

convertible into three additional Bulldog Sauce shares. However, Steel Partners and its affiliates were designated as "non-qualified persons" who could not convert the warrants into additional shares of stock but could only convert them into cash at a price equivalent to the market price of Bulldog Sauce shares at the time the plan was adopted. *Id.* at 46. When the smoke cleared, the plan coerced Steel Partners into selling three-quarters of its holding in Bulldog Sauce at the prevailing market price.

40. *Id.* at 48.

41. The shareholders' motivations become somewhat easier to understand in light of their make-up; many were *tonkatsu* (fried pork cutlet) restaurants that were loyal customers of Bulldog Sauce (a Worcestershire-like sauce) who were given or sold small lots of Bulldog Sauce stock to cement the supplier-customer relationship. For the majority of Bulldog Sauce shareholders, the stock was not a financial investment; it was symbolic of a relationship. The lots that individual shareholders held were small enough that a large premium would not have resulted in a significant financial gain in absolute terms anyway.

42. *Id.* at 53.

independent finding and deferred to the judgment of the Bulldog Sauce shareholders, 83.8% of whom had voted for the plan.[43]

Beyond the awkwardness of having to make yet another unexplained midflight correction in Article 247 doctrine—in the form of an evidentiary presumption no less—it is puzzling why the fact that approval by an overwhelming majority of shareholders led to the conclusion that the plan was valid, as opposed to the conclusion that it was simply unnecessary and beside the point. If a majority of shareholders had made it clear they did not want Steel Partners' money, Steel Partners' tender offer posed no "threat" at all to Bulldog Sauce or its shareholders to begin with. The *raison d'etre* for poison pills is that they protect shareholders.[44] If the protection was not necessary, the practical solution would have been to let Steel Partners simply proceed with its doomed tender offer. An American court, one suspects, would have wearily asked Steel Partners why they were wasting the court's time with a practically meaningless lawsuit.

While the district court made a midflight correction in Article 247, the Tokyo High Court proceeded to hijack the airplane altogether. The high court took the four discrete "abusive acquirer" categories that began as dicta in *Livedoor* and exploded them into a nativist economic philosophy completely at odds with, among other things, the basic premises of Delaware corporate law and M&A jurisprudence. Unlike the district court, the high court had no qualms about taking it on itself to make the evidentiary finding that Steel Partners was an "abusive acquirer"; in fact, it seemed to relish making the finding:

> The appellant is a US-based fund organized in the Cayman Islands, and organizers of the fund, though the facts surrounding them are unclear, have invested over $4 billion in over 30 Japanese companies, and at the same time have made moves to gain control of the target companies by means of tender offers and other devices, with the aim of eventually disposing of their investment at a profit; against the appellee, after having acquired a substantial block of shares, they moved to acquire control but were rebuffed by management . . . having the character of an organization known as an investment fund, motivated by incentive fees, a legal entity that places profit before everything, has not shown any real interest in managing the target company, has no intention of becoming involved, and after acquiring shares of the target company, it

43. *Id*. at 55.
44. *Supra* note 37.

> launched a sudden tender offer, and using any means available, is aiming exclusively to turn a short term profit by selling the company off to a third party, ultimately contemplating even selling off the company's assets, so that it can only be said that this is a creature whose only focus is profit. Moreover, those connected with the appellant, while saying that they intend to acquire the target company, instead of acting cooperatively have stirred up mischief and discomforted the target company. This being the case, the tender offer launched by those connected to the fund, having this background and set of motives, damages corporate value and the interests of all shareholders, is illegitimate and breaches the principle of good faith and sincerity, and it is proper to conclude that appellant and those connected to it are abusive acquirers.[45]
>
> A corporation is in theory an organization with the goal of maximizing corporate value for distribution to shareholders, but at the same time a corporation cannot insist on the goal of profit alone. It has a social existence, it embraces employees within it, and has external relationships with suppliers and customers through which it gains profits. Profits must be seen in the context of these other relationships with employees, customers, suppliers and the surrounding community, i.e. the corporation's stakeholders. It is not possible to view corporate value simply in terms of the corporation's own profits. Steel Partners has no interest in participating in Bulldog Sauce's management and is only interested in getting profits from increases in stock price. As such it is an abusive acquirer. Its aim is to get a majority of the company's shares, control it, and use control as a means of making a profit for itself. It has no perspective on the good management of the company and thereby in fact reduces the corporation's corporate value and reduces the economic wellbeing of other shareholders. It is wholly reasonable to discriminate against an abusive acquirer such as this. When there is a threat of this kind, a company is wholly justified in taking defensive measures.[46]

As one parses the opinion, it is hard to identify exactly what Steel Partners *did* to deserve being labeled an "abusive acquirer." The operative criteria are dished out in a rambling, almost dream-like fashion. At the

45. Tōkyō Kōtō Saibansho [Tōkyō High Ct.] July 9, 2007, 1806 SHŌJI HŌMU 40, 50.
46. *Id.* at 47.

outset of the opinion, the high court states that the question of whether the issuance of warrants is "materially unfair" needs to be analyzed "holistically," taking into account the "provenance" ("*zokusei*," literally "attributes" or "origins") of the bidder and target.[47] The expanded definition of "abusive acquirer" goes far beyond the four discrete *Livedoor* categories. Essentially any financially motivated acquirer that does not intend to manage and operate the target itself for the long haul is "abusive." The intention to sell assets or fire employees post-acquisition also appears to be indicia of "abuse," as is acting in ways to upset or discomfort target management.

The high court's decision was criticized in Japan because it espoused a view of market capitalism that was naïve, anachronistic, and xenophobic.[48] What was barely discussed was the judicial hubris the opinion reflects. The imported seeds from Delaware sown by the Kanda Committee morphed, in the hands of the high court, into an expansive and ill-defined new doctrine totally incompatible with liberal market assumptions, much broader than necessary to resolve the case before it, and founded on its own idiosyncratic and nativist world view. The high court exhibits absolutely no reservation or diffidence. This was the schizoid state of the Article 247 issue as it landed on the Supreme Court's doorstep.

B. Article 109

1. Degrees of Equality

Article 109 of the Company Law, which explicitly codified for the first time the case law principle that all shareholders be treated equally, was the other major obstacle to the Japanese poison pill. As the leading treatise on the Company Law acknowledges, the interplay between Article 109 and other provisions of the Company Law raises a series of difficult and still unresolved questions.[49] The basic policy behind Article 109 is to prevent majority shareholders from using their position to disadvantage, or in extreme cases, to dispossess or steal from, minority shareholders.[50] In an

47. *Id.* at 46.

48. *See Panel Discussion by Leading Practitioners*, NIKKEI.COM, Sept. 5, 2007, http://www.nikkei.co.jp/hensei/comp07/20070905sfa95001_05.html?p=3.

49. EGASHIRA, *supra* note 5, at 125–27.

50. Saikō Saibansho [Sup. Ct.] Aug. 7, 2007, 1809 SHŌJI HŌMU 16, 18; Keiichi Murata, *Kaishahō ni okeru kabunushi byodo gensoku (109 jō 1ko) no ishiki to kaishaku* [*The Concept and Interpretation of the Principle of Shareholder Equality in the Company Law (Article 109, Paragraph 1)*], 316 RITSUMEIKAN HOGAKU 400 (2007).

extreme case, for example, a sixty percent shareholder could cause the board to declare a dividend only to itself and not to the other shareholders. As one intuitively recognizes, this would clearly violate the principle of equality because some shareholders holding the same shares of stock would get a dividend, while others would not.

There are other provisions of the Company Law, however, that do not require strictly equal treatment of shareholders of the same class. For example, a company does not have to issue new stock pro rata to existing shareholders. It can issue stock to some and not others, and, in the process involuntarily dilute some shareholders and increase the share percentages held by others.[51] Similarly, the new Company Law now permits cash-out mergers, meaning that if a shareholder controls sixty-seven percent or more of a company, it can merge the company into another company it controls and pay cash to squeeze out the remaining minority shareholders.[52] This is unequal treatment in the sense that one shareholder gets to remain a shareholder, and the other one gets coercively cashed out (just like Steel Partners in *Bulldog Sauce*). There are other possibilities, the validity of which have not yet been tested. For example, what about a charter provision that declares all stock held by a given shareholder in excess of twenty percent as non-voting? Or that a given shareholder had two votes for each share? There are some cases that are intuitively clear and others that inhabit a complicated gray zone. Where to draw a principled line, and on what basis, is a daunting task that the Japanese courts have yet to undertake. Drawing a principled and consistent line, presumably, would require a fine analysis of the policies and values served by the rule. It would require looking at a series of concrete examples and sorting them out. The fact that the new Company Law specifically codifies the requirement of shareholder equality in black and white would, presumably, limit the flexibility of the courts creatively to work around it.

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51. Kaisha-hō [Company Law], Law No. 86 of 2005, art. 238.

52. The relevant sections of the old Commercial Code were amended in the Company Law so as to eliminate restrictions on the form of consideration that can be used in a merger. *Id.* art. 749. Formerly, only shares of the surviving corporation were valid consideration. Shō-hō [Commercial Code], Law No. 48 of March 9, 1899, art. 352; Keiko Hashimoto et al., *Corporations*, *in* JAPANESE BUSINESS LAW 118 (Gerald Paul McAlinn ed., 2007).

2. *The Kanda Committee's Formalistic Methodology*

The Kanda Committee tackled the Article 109 problem, not with a Delaware-style policy-based analysis, but with the highly formalistic approach typical in Japanese legal practice and scholarship. As it turns out, Professor Kanda himself had written extensively on the subject, and the committee's report, concluding that Article 109 does not pose an impediment to the poison pill, reflects his scholarly views.[53]

First, the report makes a distinction between stock or stock rights and external conditions attached to the stock or stock rights.[54] The idea is that it is unacceptable to discriminate in relation to stock or stock rights, but it is acceptable to discriminate in relation to *conditions* attached to the stock, because the Company Law refers specifically to stock and stock rights, not conditions attached thereto. The artificiality of this distinction becomes apparent if one thinks of a corporation owned by a sixty percent shareholder and a forty percent shareholder, both of whose shares are otherwise identical. The directors declare a dividend payable to all shareholders, but conditioned on the shareholder owning more than forty percent of the outstanding stock. Under this analysis, the forty percent shareholder has nothing to complain about. He has the same stock and stock rights as the sixty percent shareholder. He just did not meet the *conditions* required to receive a dividend.

A second concept was that of exceptions *disproving* the rule. As we have seen, the Company Law contains specific exceptions to the principle of shareholder equality. The premise that there are exceptions leads to a rather startling conclusion: the exceptions prove that the rule does not really mean what it says and can be ignored.[55] What this sleight of hand fails to answer, however, is how the vital core of the principle, which serves an intuitively compelling set of values, can survive exceptions, if exceptions prove that the entire rule is a dead letter.

Finally, the report argues that it would simply be unreasonable to interpret the principle of shareholder equality in a way that impeded the obvious benefit to "corporate value" offered by well-designed defensive arrangements of the kind recommended by the Kanda Committee.[56] This seems to be nothing more than wishful thinking that the impediment would go away. The idea that judges, or unofficial study groups, can wave

53. HIDEKI KANDA, KAISHA HO [COMPANY LAW] 65–66 (Kobundo, 9th ed. 2007).
54. Corporate Value Report, *supra* note 11, at 79, 85–86.
55. *Id.* at 85.
56. *Id.* at 85–86.

a magic wand and make legal impediments disappear when they get in the way of good results is not easy to reconcile with the rule of law.

3. The Courts Cherry Pick Professor Kanda's Arguments

The district court, clearly having researched Professor Kanda's scholarship, rejected the first and third arguments, and adopted the second. The district court rejected the first as simply *too* formalistic. Looking at the substance of the transaction, the courts correctly saw that giving shareholders free warrants was equivalent to a stock split. So, giving warrants to all shareholders except one would be the same as splitting the shares of all shareholders except one, which would clearly violate Article 109 and the principle of shareholder equality.[57] Having declined to dodge Article 109 on overly formalistic grounds, however, the district court went on to accept Professor Kanda's second argument, namely that the exceptions wipe out the underlying rule.[58]

The fact that new shares do not have to be issued pro rata to existing shareholders, the court reasoned, demonstrates the larger principle that "the Company Law treats the claim of existing shareholders to maintain their share percentages as subordinate to their right to equal treatment with respect to the economic value of their shares."[59] Going further, the fact that minority shareholders can be squeezed out in a cash-out merger shows that:

> a minority shareholder can be removed so long as such shareholder receives cash or other consideration equivalent to the value of its shares and its economic interests are thus preserved, and subject to a special vote (i.e., vote of two-thirds majority) at a shareholders meeting.
>
> When one considers the substance of these types of provisions of the Company Law (i.e., the merger squeeze-out rules), the discriminatory exercise provisions attached to the free warrants distributed to the Bulldog Sauce shareholders, even if they result in a specified shareholder (i.e., Steel Partners) suffering the disadvantage of having its share percentage reduced, at least if the warrants were authorized by a special vote at a shareholders meeting and adequate consideration was paid for the shares, [the

57. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] June 28, 2007, 1805 SHŌJI HŌMU 43, 49.
58. *Id.* at 50–51.
59. *Id.* at 50.

> discriminatory provisions] do preserve the shareholder's right to economic equality, and in these circumstances cannot be interpreted as violating the principle of shareholder equality . . . .[60]

In short, from the premises that (a) the Company Law does not give shareholders mandatory anti-dilution rights and (b) in merger situations squeeze-outs of dissenting shareholders are permitted subject to a supermajority shareholder vote and appraisal rights, the district court leapt to the quite stunning general conclusion that (c) a shareholder can be forcibly cashed out as a shareholder basically for any reason and at any time, subject only to the vote of a two-thirds' majority and payment of "adequate consideration." As a rule of substantive corporate law and basic property law, this is quite radical. Taken literally, the district court's decision implies that, located somewhere in the penumbra of the Company Law, there is, in effect, a generalized expropriation or eminent domain right against minority shareholders. Not only is the substantive result remarkable, but the path of reasoning that the court used to arrive at the destination is an all-purpose scythe that allows courts to mow down any general rule that comes bundled with exceptions.

The Tokyo High Court, perhaps even more comfortable than the district court in acting as a roving court of equity, simply demoted Article 109 to the status of a fuzzy "principle" that does not need to be strictly observed:

> The principle of shareholder equality codified in the Company Law is in the end just a principle, as evidenced by the fact that the Company Law contains provisions that are exceptions to the principle. The principle of shareholder equality is based on the legal ideal of equity, and Article 109 is nothing more than an expression of generalized ideals of equity. Therefore it is not proper to interpret the principle of shareholder equality as requiring formal equality in proportion to the content and number of shares, except where the Company Law otherwise specifically requires such equality. Even if there is discriminatory treatment of shareholders, if such discrimination is rational taking into account relevant provisions of the Company Law, then it does not violate the principle of shareholder equality.[61]

60. *Id.* at 51.
61. Tōkyō Kōtō Saibansho [Tōkyō High Ct.] July 9, 2007, 1806 SHŌJI HŌMU 40, 46.

The high court seems to be following the third line of reasoning we saw in the Kanda Committee report, to the effect that Article 109 cannot mean what it says to the extent that it stands in the way of equity, rationality, corporate value, and blocking abusive acquirers.

C. The Supreme Court's Solomonic Solution

Perhaps hesitating to air a family squabble in public, the Supreme Court's opinion never openly acknowledged the rift between the district court and high court opinions. There was no discussion of the lower court opinions, no explanation of how they differ, nor any correction of judicial error below. The Supreme Court simply rewrote its own opinion from scratch and left it to the reader to figure out where the lower courts went wrong.

The Supreme Court decision is much shorter and addresses the issues at a much higher level of abstraction than the lower courts' decisions. Most striking, whereas the two lower courts treated Articles 247 and 109 as separate and doctrinally distinct issues, the Supreme Court strategically blurs the two and applies essentially the *same* set of doctrinal conditions and definitions to both. The result the Supreme Court deftly achieved by blending Articles 247 and 109 into more or less a single doctrinal issue was both to avoid approving, if not explicitly overruling, the high court's provocative abusive acquirer doctrine on the Article 247 front, and at the same time to sharply limit the lower courts' summary demotion of the principle of shareholder equality. The key passage from the Supreme Court's opinion states:

> The principle of shareholder equality, in order to preserve the interests of each shareholder, requires that the stock owned by shareholders be treated equally as to substance and numbers. However, since it is impossible to imagine that the interests of each shareholder could be preserved if the corporation were to cease to exist or grow, when there is an identified shareholder which seeks to acquire control of the corporation, and there is reason to believe that acquisition of control by such shareholder would endanger the corporation's existence or growth, or the corporation's corporate value would otherwise be threatened, and as a result the interests of the corporation and the common interests of the shareholders are threatened with harm, even if defensive measures of a discriminatory nature are taken against the shareholder seeking to take control, so long as such measures do not violate principles of equity and are not lacking in proportionality, it cannot be said that

> this directly offends the substance of the principle. Now, on the question of whether acquisition of control by a given shareholder would harm the interests of the corporation or the common interests of the shareholders, the ultimate judgment must be made by the shareholders themselves whose interests are bound up with those of the corporation, and absent the lack of proper procedures taken at the shareholders meeting [at which the defensive measures are adopted], or the factual premises of the decision prove to be false, or fraud and the like, or the existence of a serious defect in the legitimacy of the decision, the decision of the shareholders must be respected.[62]

This passage is about Article 109. But, notice carefully, the doctrinal concepts the Supreme Court applies—corporate value, threat, proportionality, evidentiary presumption in favor of a shareholder vote—are the concepts that the Kanda Committee and the lower courts applied not to Article 109, but to *Article 247*. This seems odd, since Articles 247 and Article 109 reflect underlying policies that are different, or at least opposite sides of the same coin. As in the lower court decisions, there is no discussion of a larger policy context. The mention of "threat" and "proportionality" is a silent bow to *Unocal*, the Kanda Committee, and *Livedoor*. However, the words are ripped out of their original context and defined out of existence, in any event, by the concept that "threat" and "proportionality" mean whatever a majority of shareholders decides. What the Supreme Court did accomplish by conflating Articles 247 and 109 in this way was narrowly to limit the lower courts' overly broad Article 109 rulings. Recall that, on Article 109, the district court ruled that there was a general expropriation right lurking in the penumbra of the Company Law, while the high court demoted the principle of shareholder equality to a fuzzy rule that could be observed in the breach. The Supreme Court, by contrast, limits its holding on Article 109 to situations where there is "an identified shareholder which seeks to acquire control of the corporation" and a large number of shareholders vote to take discriminatory action against the identified shareholder—i.e., the specific facts of the Bulldog Sauce case itself. Perhaps the Supreme Court, lacking a commercial background, did not itself realize how radically this narrowed the ruling. Even in Japan, getting a majority of shareholders to vote to tell an identified bidder to "get lost," regardless of the premium offered, is likely to be a rare event. The peculiar shareholder base of Bulldog Sauce

62. Saikō Saibansho [Sup. Ct.] Aug. 7, 2007, 1809 SHŌJI HŌMU 16, 18.

accounts for what was, in effect, an aberrant, economically irrational shareholder decision. In these rare circumstances, if the shareholders vote to block a tender offer, it has no practical significance since the tender offer, if it went forward, would fail anyway.[63]

Most significantly and ironically of all, because of the way the Supreme Court narrowed the Article 109 ruling to fit the unique facts of *Bulldog Sauce*, the decision has nothing at all to say about conventional poison pills, which are adopted before an identified bidder appears on the horizon. After all the twists and turns beginning with the Kanda Committee report, the opinion does nothing to clarify the legal status of the poison pills now in place across corporate Japan. The legality of the Japanese poison pill still rests on the Kanda Committee report and a vague consensus based on comfort in the numbers of corporations that have gone ahead and adopted poison pills. The Supreme Court deftly killed a second bird by imposing the same narrow conditions on both Article 109 and Article 247: to the extent that the shareholders, rather than the courts, determine whether a "threat" exists, the courts are absolved from having to determine whether particular bidders are "abusive" or not, and the high court's flamboyant "abusive acquirer" doctrine is thereby neutralized. Significantly, though, the Supreme Court never specifically overruled the high court's "abusive acquirer" doctrine or finding. Like the district court, it simply said the court had not needed to make such a determination if the shareholders had voted. The death of the high court's nativist "abusive acquirer" doctrine therefore cannot be conclusively proved; it continues to float over the opinion like Banquo's ghost.

The Supreme Court's *Bulldog Sauce* opinion was a calculated exercise in damage control, not a bold statement of policy. It reined in the excesses of the two lower courts, but whatever substantive corporate law doctrine was left standing verged on meaninglessness. To conclude, as some have, that the Kanda Committee's report and the cases that it inspired show Japanese corporate law "converging" with that of Delaware is confusing superficial resemblance with real substance.[64]

63. Japanese academics and commentators largely took the view that the Supreme Court's decision in *Bulldog Sauce* reflected "respect for shareholders" without reflecting on the question of why shareholders need to be protected from a tender offer they have shown they will reject anyway. *See, e.g.*, Masafumi Nakahigashi, *Burudokku sōsu jiken to kabunushi sōkai no handan no sonchō* [*The Bulldog Sauce Case and Respect for Decisions made at Shareholders Meetings*], 1346 JURISUTO 17 (2007).

64. *See* Curtis J. Milhaupt, *In the Shadow of Delaware?: The Rise of Hostile Takeovers in Japan*, 105 COLUM. L. REV. 2171 (2005).

The entire episode exposes a judiciary whose comprehension of its own role and scope of authority is undisciplined, shifting, and unformed. Deciding more than necessary to resolve the case before it—as in gratuitous dicta injected in *Livedoor*, or the Tokyo High Court's out-of-the-blue reinvention of the "abusive acquirer" doctrine—seems to cause no bashfulness. Amending the applicable doctrine from case to case, or shifting the basis for decision without comment or explanation at different levels in the appellate process, are accepted as unremarkable. As the district court and high court's Article 109 decisions reveal, judges show little reserve ignoring or marginalizing statutes that get in the way of results that they believe need to be delivered.

This judicial style, which embodies broadly held Japanese mentalities shared across a range of other intellectual disciplines, ultimately reflects institutional weakness rather than strength. Manipulating doctrine low to the ground to accommodate the dominant consensus reveals not an imperial judiciary, but one that is eager to please. For the most part, judicial accommodation of the dominant consensus leaves no victims. But there are exceptions, which I take up in the conclusion of this essay.

D. Putting the "Abusive Acquirers" Out of Business: The Murakami Insider Trading Case

Although the Supreme Court sterilized the high court's "abusive acquirer" doctrine, the notion that the new breed of raider was a greedy and rapacious threat to traditional Japanese business norms and ethics continued to run strong through the establishment. In 2006, the national prosecutor's office indicted Horie and Murakami on criminal charges and put them out of business.[65] This time, failure by the courts to see the relationship between the literal words of a criminal statute and the policies served by the statute led to a shameful miscarriage of justice.

Yoshiaki Murakami was arrested in June 2006 for insider trading violations related to his fund's trading of shares of NBS, the same company whose attempt to thwart Livedoor's bid by issuing warrants to its affiliate Fuji Television a year earlier had been invalidated in the *Livedoor* decision.[66] Murakami was convicted by the Tokyo District Court in July

65. *4000 oku fando hōkai kiken Murakami daihyō taiho* [*¥400 Billion Fund on Verge of Collapse; Principal Murakami Arrested*], YOMIURI SHIMBUN, June 6, 2006, *available at* http://www.yomiuri.co.jp/atmoney/mnews/20060606mh06.htm; *Raibudoa Horie shachō taiho* [*Livedoor President Horie Arrested*], YOMIURI SHIMBUN, Jan. 24, 2006, *available at* http://www.yomiuri.co.jp/atmoney/mnews/20060124mh17.htm.

66. Livedoor v. Nippon Broad. Sys., Tōkyō Chihō Saibanscho [Tōkyō Dist. Ct.] Mar. 11, 2005,

2007 (the same month the Supreme Court took on the *Bulldog Sauce* case) and sentenced to two years of hard labor, while his fund was fined a record ¥1.149 billion.[67] The Tokyo High Court's decision to convict Murakami of insider trading dramatizes the pitfalls of applying rules mechanically without connecting the meaning of the rules to a larger factual and policy context. The Tokyo District Court framed the issues of the case at the outset:

> The facts underlying the indictment are as stated in the court's findings of fact, but among other facts, we note the defendant corporation's [Murakami Fund's] business, that the individual defendant [Murakami] is a director and effective manager of [Murakami Fund], that between November 9, 2004, and January 26, 2005, through [Lehman Brothers] and other intermediaries, purchased 1,933,100 shares of [NBS] stock, and on November 8, 2004, [Murakami] admits he unmistakably heard from [Horie] that he [Horie] was interested in acquiring control of [NBS], but thought that it was just big talk and an exaggeration, that [Murakami] had been acquiring stock of [NBS] well before in anticipation of a proxy fight, and did not acquire additional shares of NBS based on gaining information that [Livedoor] intended to acquire NBS shares on a large scale, and that he [Murakami] is therefore innocent.[68]

At the outset, the statute that Murakami was accused of criminally violating, Article 167 of the Securities Law, is nowhere identified, nor are the facts relevant to his guilt under the statute.[69] The questions, "How did he violate the statute?" and "Who was actually hurt?" are never addressed. Indeed, Article 167 is mentioned for the first time more than halfway through the forty-page opinion, and then only partially and in passing.[70] The court, having "framed" the issues, then proceeds to recount various facts, beginning with the formation of the Murakami Fund and continuing through Murakami Fund's acquisition of NBS shares starting in 2003, Murakami's heavily publicized campaign against NBS management,

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67. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] July 19, 2007 (*Murakami Insider Trading*) (unpublished), *available at* http://www.westlawjapan.com/case_law/pdf/WLJP_10-01-2008_04_22.pdf.

68. *Id.* at 2–3.

69. KINYŪ SHŌHIN TORIHIKI-HŌ [FINANCIAL INSTRUMENTS AND EXCHANGE ACT], Law No. 25 of 1948, as amended by Law No. 109 of 2006, art. 167.

70. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] July 19, 2007 (*Murakami Insider Trading*) (unpublished), *available at* http://www.westlawjapan.com/case_law/pdf/WLJP_10-01-2008_04_22.pdf.

followed with accounts of meetings with Horie in late 2004 in which Murakami encouraged Horie to make his own bid for NBS.[71] Without any indication from the court as to what exactly Murakami's crime consisted of, an ordinary reader is at a loss to decipher which of the many facts bear upon Murakami's guilt. The decision lacks an anchoring thesis.

To fill in the context missing in the decision itself, Article 167 of the Japanese Securities Exchange Law somewhat cryptically expresses a rule analogous to Rule 14e-3 under the U.S. Securities Exchange Act that, in essence, prohibits trading in a company's shares if the trading party knows that an unannounced tender offer will be launched for the company's shares.[72] The basic policy objectives of both rules is clear: to prevent parties who discover the existence of a planned tender offer before it is announced from getting an unfair "jump on the market" and locking in an undeserved tender offer premium ahead of the announcement.[73]

Murakami ran afoul of Article 167 because, on November 8, 2004, he visited Horie and encouraged him to launch his own tender offer for NBS.[74] Horie indicated he was definitely interested, but still unsure whether he could arrange the necessary financing.[75] Horie begged Murakami to hold on to, and not sell out, the eighteen percent of NBS that Murakami had already amassed; Horie was counting on Murakami's eighteen percent, to add to the thirty-three percent plus that Horie hoped to acquire himself, to add up to majority control of NBS. Murakami replied, "I can't promise anything, but trust me."[76] Based on this conversation, the prosecution alleged that Murakami "knew" that Horie/Livedoor were committed to launching a tender offer for NBS.[77] Therefore, any trading that Murakami did in NBS shares between the date of the conversation, November 8, 2004, and the date that Horie announced his position in NBS on February 8, 2004, was tainted and in violation of Article 167.[78]

The prosecution and Murakami's lawyers, and subsequently the court, narrowed the relevant legal issue to whether Murakami had sufficient "knowledge" of Horie's intention to launch a tender offer based on what

71. *Id.* at 3.
72. 17 C.F.R. § 240.14e-3(a).
73. Tender Offers, 45 Fed. Reg. 60411 (Sept. 12, 1980) (to be codified at 17 C.F.R. pt. 240) (Securities and Exchange Commission announcement promulgating Rule 14e-3).
74. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] July 19, 2007 (*Murakami Insider Trading*) (unpublished), *available at* http://www.westlawjapan.com/case_law/pdf/WLJP_10-01-2008_04_22.pdf.
75. *Id.*
76. *Id.*
77. *Id.* at 27–28.
78. *Id.* at 36.

was communicated at the November 8th meeting.[79] Murakami argued that Horie's statement that he was "definitely interested" was not an unequivocal commitment and that Horie's ability to line up financing was very much in doubt.[80] The court, having accepted this narrow definition of the issues, proceeded to find that Murakami did in fact have the requisite knowledge and convicted him.[81]

What escaped the court, and to some extent Murakami's own lawyers, was the factual and practical commercial context as it related to the meaning and purpose of Article 167. Murakami was by no means a typical inside trader, lurking in the shadows and abusing nonpublic information about a company that no one suspected was in play. To the contrary, it was Murakami himself who had invited a control contest for NBS in 2003, publicly announcing and disclosing his growing position in the company, making loud statements that he thought the stock was undervalued, and urging NBS's affiliate and largest shareholder, Fuji Television, to make its own tender offer and convert NBS into a subsidiary.[82] As a result of Murakami's public campaign, NBS's stock price rose from ¥2730 in January 2003 to ¥4880 in November 2004.[83] In other words, Murakami himself, by completely legitimate methods, had already exposed NBS's hidden value to the benefit of its shareholders. Thanks to Murakami, it was public knowledge that NBS was in play and that Fuji Television or a third party could make a tender offer at any moment. Indeed, it was Fuji Television's tender offer bid of ¥5950 on January 17, 2005, not any action on the part of Horie, that caused the next spike in NBS's stock price.[84] It would be hard for an investor to claim that, if he had known that Horie would launch a tender offer, he would have bought more NBS stock. In a general sense, the information was already well known.

The other critical fact overlooked by the court was that *before* Horie announced that he had acquired thirty-five percent of NBS on February 8, 2005—and therefore before any impact on stock price attributable to Horie—Murakami had already sold his position *to Horie himself*. In a classic double cross, Murakami covertly sold Horie, in the anonymous

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79. *Id.* at 22.

80. *Id.* at 23.

81. *Id*. at 36.

82. *Murakami Fando, nippon hōsō no dai-ni kabunushi ni—kaimashi de 7.37% hoyū* [*Murakami Fund Becomes Second Largest NBS Shareholder—Holds 7.37% as a Result of Increased Share Percentage*], NIHON KEIZAI SHIMBUN, July 17, 2003, at 17.

83. Robin Greenwood & Michael Schor, *Livedoor*, Harvard Business School Case Study No. 9-206-138, at exhibit 3 (2006).

84. *Id.*

after-hours market, the very shares that Horie had begged Murakami to hold on to. Horie gleefully announced he had acquired thirty-five percent of NBS on February 8, 2005, still thinking that in combining his shares and Murakami's eighteen percent, he had acquired control of NBS. Horie received a jolt at the end of February when Murakami's filings with the FSA showed that Murakami had made a grand exit from NBS and that Horie was the dupe.[85] If there was any victim of Murakami's "insider trading," it was Horie.

Murakami arguably violated the literal words of Article 167. However, he did not offensively violate its spirit. He would have made the same trades whether or not he had "known" that Horie would make his own bid. Nonetheless, echoing the Tokyo High Court's "abusive acquirer" doctrine, the Tokyo District Court, without a good grasp of the commercial context, justified a two-year prison sentence based solely on the fact that Murakami's transactions were motivated by profit:

> It is clear that Murakami's only motive from the beginning was to wring as much profit from the situation as possible, and that was his only motive in using insider information. This is a critical factor in determining the defendant's sentence. One may casually think that his actions are less serious and malicious than a case of a true "insider," but Murakami used his position as chairman of a major investment fund to launch a proxy fight demanding "reforms" he had no genuine interest in seeing, other than to the extent they might result in greater profit for him. He must be punished for his extreme greed.[86]

Just as the Supreme Court put a brake on the excesses of the lower courts in *Bulldog Sauce*, a year-and-a-half later, the Tokyo High Court itself corrected the district court's effort to criminalize Murakami's "greed."[87] By then, it had become clear that the new breed of raider was a limited phenomenon and posed no real threat to the corporate establishment. Collective second thoughts about the impulsiveness and harshness of the treatment meted out to Murakami and Horie had begun to

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85. *Murakami Fando—nippon hōsō kabu, 3 gatsu 6% hoyū, jōjō haishi kenen tsuyomaru* [*Murakami Fund—Down to 6% of NBS at End of March—Fears of Delisting Increase*], NIHON KEIZAI SHIMBUN, Apr. 16, 2005, at 11.

86. Tōkyō Chihō Saibansho [Tōkyō Dist. Ct.] July 19, 2007 (*Murakami Insider Trading*) (unpublished), *available at* http://www.westlawjapan.com/case_law/pdf/WLJP_10-01-2008_04_22.pdf.

87. Tōkyō Kōtō Saibansho [Tōkyō High Court] Feb. 13, 2009, 1299 HANREI TAIMUZU [HANTA] 99.

surface. The Tokyo High Court's effective reversal of the criminal sentence handed down by the district court, which received scant publicity, reflects a different collective mood from the received wisdom that prevailed two years earlier:

> If we impose criminal penalties that are overly severe on the kinds of market activities described above [i.e., Murakami's transactions in NBS stock], facts which are not even the subject of the indictment may become crimes. . . . The Murakami Fund, viewed in another light, can be seen as attempting to reform the practices of companies it invests in (so called shareholder activism), and we do not believe that a mature discussion has yet been completed on that subject. The defendant did not from the beginning intend to use insider information for personal gain, nor was he strongly conscious that he in fact possessed insider information; we do not believe that he acted in the conscious belief that he was violating law; or that the great majority of the shares he acquired which were subject to the indictment were acquired with this consciousness; these facts must, in the end, be taken into consideration in determining his criminal state of mind.[88]

One of the basic functions of a judiciary ought to be to distinguish between the letter and spirit of rules in a mature and independent way. To do so necessarily requires understanding the meaning of rules against a real-world context of facts and the policies, principles, and values served by the rules in question. The reaction of the Japanese courts to Steel Partners, Murakami, and Horie displays an uncritical willingness to serve a received consensus by applying and manipulating the surface and letter of rules, without inquiring more deeply into the meaning and purpose of the rules. Although it is foolhardy to expect that Japanese judicial opinions will ever read as if they were penned by Justice Scalia or Judge Posner, Japan should welcome a more skeptical, autonomous, and rigorous judiciary to serve as a check against the shifting tides of consensus.

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88. *Id.*