CHAPTER III

The Primary Stock Market

1. Corporations and Shares

For the purp-ose of the Companies Act, companies are classified into corporations (*kabushiki kaisha*); general partnerships (*gomei-gaisha*); limited partnerships (*goshi-gaisha*); and limited liability companies (*godo-gaisha*). Of these, corporations have a number of advantages compared to other types of company in that (1) ownership interest in a company is divided into shares of stock; (2) investors may recoup contributed capital simply by selling their shareholdings; and (3) investors shall be held liable only to the extent of capital contributed by them (limited liability). These advantages help a corporation to raise a large amount of capital from various investors.

The shares issued by a corporation are capital securities, or narrowly defined securities, in that they represent certain claims and rights of their investors. Shareholders contribute capital in exchange for their shareholdings, which give them privileges to (1) participate in the management of the corporation (by attending general shareholder meetings and exercising voting rights that are proportionate to their shareholdings); (2) claim distribution of profits; (3) claim residual corporate assets; and (4) file derivative suits. Issued shares, unlike bonds, are not redeemable except when shares are repurchased by the corporation or upon liquidation. Because contributed equity may not usually be repaid by the corporation, shareholders wishing to monetize their holdings can only do so by selling them in the market. In order to increase liquidity, stock is divided into a standard unit of shares and often represented by share certificates. On the other hand, with corporate bonds, another class of capital securities, the repayment value is backed by the issuing company.

The legal framework for stocks has undergone substantial changes through a series of amendments to the Commercial Code introduced since 2001. Pursuant to the amendments that took effect on October 1, 2001, par value stock was abolished and all stocks are now issued with no par value. Accordingly, the par value-based *tan'i-kabu* round-lot system was replaced by the new, discretionary *tangen-kabu* system. Under the amendments enforced on April

Table III-1. Principal Rights of Shareholders

Rights for personal interest (rights on benefits of owing property)	Rights for common interest (rights on participating in management)
・Right to claim dividend of surplus ・Right to subscribe for new shares ・Right to demand distribution of residual assets ・Right to request registration of name transfer ・Right to request purchase of shares	・Right to exercise votes at general shareholder meetings ・Right to bring representative suit ・Right to convoke a general shareholder meeting ・Right to demand suspension of illegal action by a director ・Right to make a shareholder proposal ・Right to request dissolution ・Right to demand dismissal of a corporate officer ・Right to request inspection, etc.

Table III-2. Recent Amendments to the Commercial Code Relating to Equity Financing and Main Contents of the Companies Act

The amendments made in 2001 (enforced on October 1, 2001):
A revision of the system of acquiring and holding one's own shares (the ban on holding treasury shares was lifted); the abolition of the system of issuing shares with face value (under this system, all shares are issued without par value); the abolition of the requirement of net asset value (a minimum of ¥50,000 or $487.8 at the rate of ¥102.50 to the dollar); the abolition of the *tan'i-kabu* system in favor of *tangen-kabu* system; and the relaxation of the legal reserve system, etc.

The amendments made in 2001 (enforced on April 1, 2002):
The institution of the equity warrant system and the abolition of regulation of the stock option system, the electronification of corporate documents, and a revision of regulation of the classified stock (the lifting on the ban of tracking stock*), etc.

The amendments made in 2002 (enforced in April 2003):
A revision of regulation of the classified stocks, the institution of the system relating to lapses of stock certificates, and the rationalization of the procedure for reducing capital, etc.

The amendments made in 2003 (enforced on September 25, 2003):
The acquisition of one's own shares by a resolution of the board of directors under the provisions of the articles of incorporation and a revision of the method of computing a limit on interim dividends, etc.

The amendments made in 2004 (enforced on October 1, 2005):
The adoption of a system of not issuing stock certificates, the introduction of a system of issuing notices by electronic means, etc.

Amendments in conjunction with the enactment of the Companies Act in 2005 (enforced on May 1, 2006):
A revision of regulations to make the share transfer system more flexible, the rationalization of the system of retiring shares, a revision of regulations relating to issuing of share certificates, and the abolition of fractional shares, etc.

The amendments made in 2014 (enforced on May 1, 2015):
Revision of new share issuance procedure involving transfer of controlling shareholders Introduction of a cash-out method that allows a special controlling shareholder to request other shareholders to sell their shares, etc.

The amendments made in 2019 (enforced on March 11, 2021):
Founding the system of share delivery

Note: The ban on tracking stock (under this system, dividends are paid not out of the earnings of a company as a whole but out of the earnings of a specific division or a subsidiary of such company) was lifted.

1, 2002, (1) new subscription rights/warrants were introduced; (2) the regulation of stock options was relaxed; and (3) the regulations on class shares were relaxed. The Commercial Code as amended in 2004 and the Law Revising the Act on Book Entry of Corporate Bonds and Shares, etc. for Streamlining Settlement of Transactions in Stocks, etc., introduced a no-share-certificate system. As a result of the revision of the Companies Act, share certificates of public companies were dematerialized from January 2009. Transfer restrictions on any and/or all classes of stock and issuance of classified stocks subject to wholly call were put in place in May 2006, and a cash-out system allowing a Special Controlling Shareholder to require other shareholders to sell their shares was introduced in May 2015. The amended Companies Act of 2019 introduced a new stock delivery system as a way for companies to acquire other companies in exchange for their own shares (effective March 2021).

2. Forms of Issuing New Shares

Shares are first issued when a corporation is established. Establishment of a corporation can be roughly divided into incorporators-only establishment and by-subscription establishment. When a corporation is established only with the funds contributed to its capital stock by its promoters, this method of establishing a corporation has the advantage of its shares being fully subscribed to, but it has a drawback in that the number of shares it can issue is limited to the funds its promoters can raise. On the other hand, establishing a corporation with the capital raised by publicly offering its shares to an unspecified large number of investors is called "establishment through a public offering of shares." While a large amount of capital can be raised through this method, one major drawback is that it takes time to successfully complete the public offering, and if its shares are not fully subscribed to by investors during the public offering period, the corporation cannot be established. Under the old provisions of the Commercial Code, the issue price of shares issued by a corporation at the time of establishment had to be ¥50,000 or more, but this restriction was abolished by virtue of the 2001 amendment to the Commercial Code.

Even after a corporation is established, it is a general practice for a corporation to issue new shares in order to raise funds, transfer control of its management to a third party, or to enhance the liquidity of its shares. Usually, the method of issuing new shares is divided into paid-in capital increase and stock splits (and gratis issues). Issuing new shares against the payment for them by shareholders is called a paid-in capital increase, and a corporation can raise equity capital by this method. Paid-in capital increases are also di-

Table III-3. Forms of Issuing New Shares

Payment required
Capital increase through a public offering
Capital increase through a third-party allocation of new shares
Capital increase through a rights offering
The exercise of subscription rights/warrants
Payment not required
Stock split
Merger
Swap of shares
Stock transfers
Share delivery

Table III-4. Funds Raised by Equity Financing

(100 million yen)

Year	Rights offering		Public offering		Third party allotment		Exercise of subscription rights/warrants		Preferred stock and others		Total	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
2000	2	82	24	4,941	46	9,228	87	1,056	4	1,073	163	16,381
2001	3	320	18	12,015	57	4,772	85	374	5	2,161	168	19,642
2002	0	0	19	1,533	62	4,844	78	2,763	36	9,968	195	19,107
2003	2	15	35	5,672	84	2,232	121	366	74	25,322	316	33,607
2004	1	27	78	7,502	129	5,726	228	995	50	13,626	486	27,877
2005	2	37	74	6,508	150	7,781	336	1,669	45	11,678	607	27,673
2006	0	0	69	14,477	145	4,165	371	1,513	26	5,597	611	25,751
2007	1	81	60	4,570	117	6,621	347	1,650	12	7,955	537	20,877
2008	1	1	27	3,417	93	3,958	240	209	9	5,937	370	13,523
2009	0	0	52	49,668	115	7,146	169	188	28	4,740	364	61,743
2010	1	7	50	33,089	88	5,356	159	246	10	736	308	39,433
2011	0	0	45	9,678	66	3,952	171	261	7	693	289	14,584
2012	1	4	53	4,518	71	1,593	174	218	17	12,755	316	19,088
2013	1	10	114	11,137	151	3,719	350	1,904	3	1,200	619	17,970
2014	0	0	129	13,780	190	3,928	412	1,087	14	2,242	745	21,037
2015	1	1	131	9,620	187	1,635	437	815	6	7,513	762	19,583
2016	1	2	95	2,577	151	6,230	483	901	7	1,480	737	11,191
2017	2	1	116	4,242	238	8,816	526	1,926	7	613	889	15,599
2018	0	0	129	4,016	303	2,146	597	2,277	6	595	1,035	9,034
2019	0	0	93	2,198	307	9,104	572	1,431	10	1,508	982	14,241
2020	1	4	108	7,328	342	4,042	624	2,203	11	1,947	1,086	15,524
2021	1	2	159	13,692	467	17,791	709	2,235	36	1,612	1,372	35,332
2022	1	1	85	1,293	440	2,733	665	1,239	18	630	1,209	5,895
2023	0	0	107	5,887	474	3,277	686	1,638	11	3,946	1,278	14,748
2024	0	0	97	5,730	492	3,263	709	1,986	12	3,238	1,310	14,218

Source: Website of the Tokyo Stock Exchange.

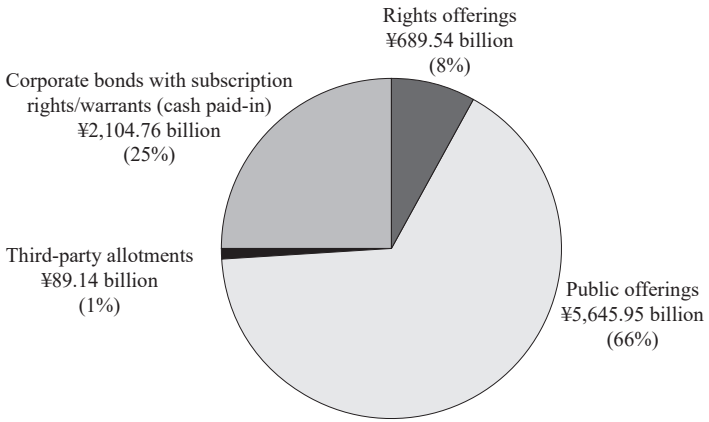
vided on the basis of investors to whom shares are issued into public offerings, rights offerings, and allotments of new shares to a third party. By definition, a stock split, the act of splitting one share into two or more shares, does not by itself increase the assets or the capital of a corporation. However, new shares issued via a stock split play an important role. The stock split increases the number of the corporation's shares in issue, and the resultant fall in the price per share enhances liquidity, making it easier to raise funds through equity financing in the future. Until 2001, there was a rule banning any stock split that reduces the value of net assets per share to less than ¥50,000, but this rule was abolished by virtue of the 2001 amendment to the Commercial Code. This step was taken because of widespread complaints among venture businesses—those that have high growth potential and whose shares are traded at high prices despite limited net assets—that on account of the restrictions on stock splits, they could not improve the liquidity of their shares. However, it was desirable to prevent share certificates from being in short supply during the period from the record date of stock split (day on which the shareholders to whom new shares are allocated are determined) to the effective date (day on which shareholders' rights to new shares go into effect), which can disrupt the demand-supply balance and cause stock prices to fluctuate violently. Hence, it was decided that the effective date would fall on the day following the record date from January 2006.

Other cases in which a corporation is authorized to issue new shares include the exercise of new share subscription rights/warrants, a new type of warrant introduced by the amendment to the Commercial Code that took effect in April 2002; share exchanges with the shares of a company becoming a subsidiary under the share exchange system; allocation of shares to shareholders of a subsidiary under the stock transfer system; and the newly introduced share delivery system.

3. Procedures for Issuing New Shares

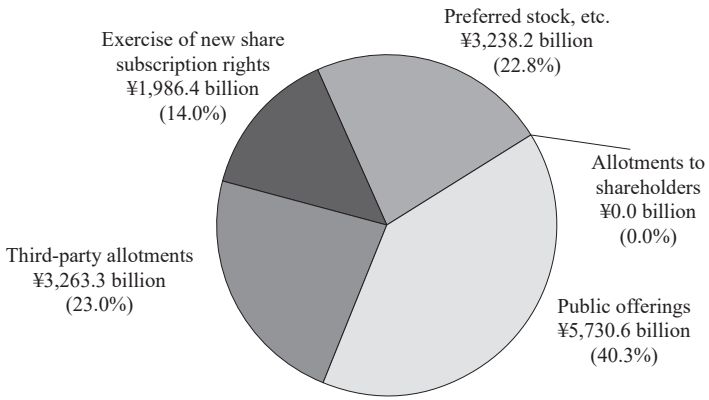
New shares can be issued in exchange for capital paid in by investors in the form of a public offering, third-party allotment, or rights offering. In a rights offering, registered shareholders as of a specified record date are given subscription rights in proportion to their stockholdings. In the case of public companies, the grant of subscription rights or allotment of new shares to nonshareholders are subject to board approval. Under the Companies Act, a shareholder allotment by a private company, in principle, requires a special resolution at the general shareholders meeting, but it may be conducted by ordinary resolution when provided for in the Articles of Incorporation. A rights offering to existing shareholders is a means of capital raising that is

Chart III-1. Equity Financing in 1989 by TSE-Listed Companies, by Type of Financing (Total capital procured: ¥8,529.39 billion)



Source: Tokyo Stock Exchange, *the Tosho tokei geppo* (TSE Monthly Report).

Chart III-2. Equity Financing in 2024 by TSE-Listed Companies, by Type of Financing (Total capital procured: ¥14,328.5 billion)



Source: Web page of the Tokyo Stock Exchange.

neutral to the control of corporations, in that it does not affect proportionate ownership of the shareholders. An offering of rights at par used to be the principal measure of equity financing, but these offerings are no longer common, partly due to the elimination of par value of stocks under amendments to the Commercial Code in 2001. Public offerings grant subscription rights to the general public. A public offering raises more capital for an issuing company with the same amount of shares than an offering of rights at par under the par value system at the time based on the premium of the issue price over par. From the viewpoint of investors, however, it deprives investors of the opportunity to earn the premium, thereby losing their incentive to subscribe. Although public offerings declined in the 1990s, they are now the primary means of raising equity capital today. A third-party allotment raises capital by granting subscription rights to certain third parties, including banks or business corporations with special relationships with the issuing company and/or its director(s). This method is often used to bail out troubled companies, strengthen relationships with corporate partners, and form a business and capital alliance rather than simply to raise capital. Additionally, the method has recently been noted as a measure for fending off hostile takeovers. Third-party allotments cause dilution of ownership of existing shareholders. These may be approved by board resolution except when shares are allotted at a price particularly favorable to the grantee(s) compared with the market price. In such a case, a special resolution by the general shareholders meeting is required because it would harm the interests of existing shareholders (advantageous issuance). An issuing company pursuing a capital increase by third party capital allocation has an obligation to explain the rationale and necessity of the capital increase in its securities registration statement.

Under the revised Companies Act of 2014, which took effect in 2015, when the issuance of new shares by a public company results in a change in the controlling shareholder (holding one-half or more of the voting rights), the name and other information of the subscriber must be notified to existing shareholders. Furthermore, if there is opposition by 10% or more of voting rights, the share issuance is subject to a resolution not only by the board of directors but also by the general shareholders meeting. This strengthens the involvement of shareholders in share issuance.

4. The Current State of the New Issue Market

New shares are usually issued (1) in exchange for capital contribution (equity financing in the form of public offerings, third-party allotments, rights offerings, exercise of subscription rights, etc.); (2) in conjunction with stock splits (and gratis issues); and (3) for the purpose of corporate acquisitions. (Share

Table III-5. The State of Issuing New Shares by Listed Companies

(in thousands of shares)

Year	Paid-in capital increase	Rights offering	Public offering	Third party allotment	Preferred stock, conversion of a corporate bond with subscription rights/ warrants of the convertible bond type into shares, etc.	Subscription rights/warrants	Stock split	Others	Total
1984	5,312,713	1,170,322	778,686	319,665	2,835,670	208,370	4,033,612	169,830	9,516,159
1985	5,580,645	909,635	590,696	118,126	3,514,706	447,179	4,390,653	93,169	10,064,468
1986	4,503,842	371,191	346,883	78,308	2,831,297	876,161	3,939,802	621,924	9,065,569
1987	8,600,184	547,900	718,327	314,650	4,753,694	2,265,611	3,300,518	510,942	12,411,644
1988	9,052,096	849,464	1,286,177	169,633	4,623,233	2,123,587	4,004,200	96,212	13,152,509
1989	12,467,106	803,396	3,558,558	94,151	5,522,653	2,488,346	5,906,047	44,848	18,418,003
1990	4,733,374	758,546	1,284,250	252,593	1,859,145	578,839	8,283,600	1,632,879	14,649,854
1991	1,604,596	420,553	39,850	182,776	600,930	360,485	3,451,047	1,581,058	6,636,703
1992	766,227	244,895	2,180	190,340	139,205	189,605	1,584,403	414,121	2,764,752
1993	1,605,059	87,091	4,150	479,440	347,764	686,612	901,948	1,147,000	3,654,008
1994	1,530,474	24,152	33,360	543,846	445,479	483,635	2,330,679	1,190,447	5,051,602
1995	1,433,831	249,876	10,400	490,557	343,684	339,311	1,015,654	359,334	2,808,819
1996	2,546,611	455,200	200,883	583,427	506,753	800,348	847,835	1,873,163	5,267,610
1997	3,093,475	204,686	93,250	1,493,319	1,034,959	267,261	551,076	251,712	3,896,265
1998	3,641,490	7,707	97,337	2,380,126	1,079,024	77,295	168,263	22,696	3,832,450
1999	9,627,895	–	54,599	8,402,531	976,593	194,170	742,946	61,952	10,432,793
2000	3,709,565	87,140	84,200	2,621,987	835,744	80,492	1,599,465	1,158,762	6,467,792
2001	4,526,944	143,051	49,760	3,328,896	935,912	69,324	624,199	3,330,016	8,481,160
2002	4,260,986	–	238,268	2,719,749	546,153	756,815	692,917	1,412,881	6,366,784
2003	4,541,171	20,352	431,517	2,995,729	679,841	413,729	333,448	5,931,549	10,806,168
2004	5,659,174	18,193	516,166	1,586,466	2,404,691	1,133,656	2,975,260	24,497	8,658,931
2005	11,393,111	53,120	616,574	2,957,298	6,241,871	1,524,246	3,051,215	△13,967,015	477,311
2006	7,459,697	–	1,638,972	850,680	4,450,694	519,349	6,713,875	△1,201,938	12,971,634
2007	5,341,133	80,862	409,532	1,521,236	2,928,468	401,032	11,749,106	△3,504,021	13,586,219
2008	3,542,021	6,998	687,868	1,549,130	1,119,159	178,863	120,552	△542,754	3,119,819
2009	22,418,250	–	12,049,714	3,192,219	6,846,482	329,833	16,193,816	238,890	38,850,955
2010	10,464,418	68	7,548,008	1,935,650	835,992	144,697	877,229	△860,938	10,480,708
2011	6,391,284	–	2,947,644	2,283,962	839,211	320,465	1,842,238	625,267	8,858,789
2012	4,309,521	34,504	2,371,349	663,776	1,024,399	215,492	3,759,441	576,904	8,645,867
2013	5,226,016	613	1,244,084	2,058,111	1,400,302	522,905	27,099,251	△8,996,091	23,329,176
2014	4,624,642	–	1,422,172	627,019	1,933,058	642,391	8,841,942	△6,101,224	7,365,361
2015	3,717,412	1,560	679,898	767,728	1,797,390	470,834	7,060,155	△12,958,857	△2,181,288
2016	5,403,536	3,699	140,825	4,152,569	798,326	308,115	2,232,113	△29,020,941	△21,385,291
2017	4,747,915	1,312	320,095	2,934,439	606,854	885,214	4,836,899	△71,033,038	△61,448,223
2018	2,380,544	–	251,482	572,821	323,032	1,233,208	4,567,464	△26,497,834	△19,549,824
2019	4,691,381	–	110,331	3,895,668	59,353	626,026	6,495,653	△5,056,466	6,130,569
2020	2,955,070	6,155	338,199	1,380,132	214,293	1,016,292	7,360,701	△25,389,212	△15,073,440
2021	3,209,240	1,131	731,719	838,352	310,522	1,327,515	18,870,342	△2,441,419	19,638,164
2022	1,683,949	269	87,458	479,437	594,731	522,053	5,199,521	△4,241,371	2,642,091
2023	5,762,571	–	689,182	3,097,458	1,010,208	965,722	106,479,133	△4,420,084	107,821,620
2024	2,365,526	–	420,250	384,546	481,566	1,079,163	95,382,164	△6,342,605	91,405,085

Source: Tokyo Stock Exchange, *Shoken tokei nenpo* (Annual Securities Statistics) and *Tosho tokei geppo* (TSE Monthly Report).

counts are reduced when treasury stock is cancelled.) In 2024, the leading source of new shares issued by listed companies was stock splits and gratis issues (increase of 95.38 billion shares), followed by the exercise of new share subscription rights (1.08 billion shares). The amendments to the Commercial Code in 1991 defined stock splits to cover stock dividends, gratis issues and reclassification of paid-in capital in excess of par into capital stock, all of which did not involve payments by investors at the time of issuance of new shares.

Today, in Japan, equity financing is the leading source of new shares. Listed companies on the Tokyo Stock Exchange (TSE) raised approximately ¥1.4 trillion in equity in 2024. By contrast, equity financing, except for initial public offerings, is less used in the United States and the United Kingdom because it tends to dilute existing shareholders' ownership interests and consequently pushes down the stock price. It should be noted, however, that over the past years, equity financing in Japan has undergone many changes. During the period of rapid economic growth, corporations mostly used the method of rights offering at par to raise equity capital because investors did not have enough accumulation of financial assets, while issuing companies suffered a chronic shortage of funds (stock par value was abolished in 2001). In those days, corporations mostly relied on bank borrowings for their funding requirements, and the stock market was a marginal marketplace for raising capital. However, as the economy slowed after the oil shocks, the funding needs of businesses were reduced, and due in part to the necessity of securing a strong stockholder base, public offerings at market price became the prevalent means of raising equity among business corporations. Meanwhile, rights offerings also shifted from rights offering based on par value to offerings based on a median of par and market values. In the second half of the 1980s, with progress in deregulation concerning debt financing, issuance of convertible corporate bonds and corporate bonds with subscription rights/warrants increased, as did their conversion and exercise. Particularly, as banks came under pressure to meet Tier 1 capital requirements imposed by the Basel regulatory standards, they scrambled to shore up their capital base, and such issuance accounted for about half of equity financing at the time.

In the 1990s, there was a marked decline in public offerings because of stagnant stock prices, and increasing capital through public offerings remained stagnant thereafter. However, following the global financial crisis which started in 2008, equity financing picked up in 2009 as companies sought to shore up their weakened financial bases by public stock offerings. From 2015 to 2020, the total number of shares outstanding decreased due to factors such as a high level of share buybacks and cancellations. Since then, however, the number has resumed an upward trend. In recent years, the exercise of subscription rights/warrants has been relatively active, while stock

splits have remained at a high level in response to the Tokyo Stock Exchange's request to reduce trading units and minimum investment amounts.

5. New Share Underwriting

The method of issuing shares may be divided into direct offering and indirect offering, and public offering and private placement. When the issuing company itself performs the administrative procedures necessary for issuing shares and sells them to investors, this is called "direct offering (or self-offering)." Although this method helps the issuing company save the fees payable to an intermediary, it is not an easy task to perform the technically complicated procedures and sell the securities to an unspecified large number of investors. When the issuing company commissions a specialist intermediary to handle the public offering of its shares, this is called "indirect offering." The intermediary provides the issuing company with expert advice, handles the distribution of shares and performs the necessary administrative procedures on behalf of the issuing company, and takes over the shares remaining unsold after the public offering period. At present, almost all shares are offered through the indirect offering method. A "public offering" is the public solicitation of an unspecified large number of investors for the purchase of new shares, while a "private placement" is the private solicitation of a specified small number of investors. In public offerings of new shares, indirect offering through underwriting securities companies is the general rule.

In the case of an indirect offering, the issuing company concludes an underwriting agreement with a securities company. Underwriting agreements are divided into standby underwriting (the underwriting securities company commits itself to buying up any shares remaining unsold) and firm commitment underwriting (it agrees to buy up the entire issue from the start). Today, the latter has become the general practice. When the total amount of shares offered is too large, a single securities company cannot accept the underwriting risk involved. Therefore, multiple securities companies form an underwriting syndicate together. Of these securities companies, the firm that plays the leadership role in organizing the syndicate members and in negotiating the terms and conditions of the underwriting agreement with the issuing company is called the "lead underwriter." The group of securities companies that assumes no underwriting risk and only sells the securities is called the "selling group."

In a public offering or secondary distribution, it is necessary to have a strategy for balancing supply and demand. Using an over-allotment option allows the securities company acting as the lead underwriter of an offering to borrow shares from existing shareholders and sell them if demand exceeds

Table III-6. Number of Lead Managing Underwriters in Shares of Securities Companies (IPOs)

(Existing stock exchanges and start-up markets in 2024)

Securities companies	Prime		Standard		Growth		Other regional markets	
	No. of co.	% of total	No. of co.	% of total	No. of co.	% of total	No. of co.	% of total
Nomura	3	75.0	4	30.8	7	10.9	–	–
SMBC Nikko Securities	1	25.0	2	15.4	19	29.7	–	–
Daiwa	–	–	4	30.8	9	14.1	–	–
Mizuho	–	–	1	7.7	13	20.3	–	–
SBI	–	–	1	7.7	10	15.6	–	–
Tokai Tokyo	–	–	1	7.7	3	4.7	–	–
Mitsubishi UFJ Morgan Stanley	–	–	–	–	2	3.1	–	–
Okasan	–	–	–	–	1	1.6	1	20.0
J Trust Global	–	–	–	–	–	–	3	60.0
Aizawa	–	–	–	–	–	–	1	20.0
Total	4	100.0	13	100.0	64	100.0	5	100.0

Source: PRONEXSUS, *Kabushiki Kokai Hakusho* (White Paper on Public Listings).

Table III-7. Flow from additional secondary distribution by over-allotment in initial public offering to syndicate cover transaction



Board of directors' meeting on issuance of new shares and secondary distribution
Set OA offering limit

Determine provisional terms

BB (Report demand)

Set open price
Set OA offering volume

Listing date (Trading start date)

SC transaction or GS exercise

BB = Book Building
OA = Over-Allotment
SC transaction = Syndicate Cover (short cover) transaction
GS exercise = Exercise of Green Shoe option

Note: SC transactions and exercise of GS must be executed within 30 days from the day following the date on which the period during which investors submit their applications to securities companies is completed (normally, 2 or 3 business days prior to the listing date).

the original scheduled number of shares. In Japan, the over-allotment option has been available for offerings in which the lead underwriter enters into an underwriting agreement, beginning with offerings for which such agreements were concluded on or after January 31, 2002. This option allows the sale of additional shares up to 15% of the scheduled number of shares in the public offering or secondary distribution. The way in which the short position arising from the lead underwriter utilizing the over-allotment option is closed out varies depending on whether the price in the secondary market has risen or fallen compared with offer price. If the price of the shares has fallen, the lead underwriter purchases the excess shares in the secondary market (syndicate cover). When the price of the shares has risen, the lead underwriter exercises a green shoe option (right to acquire additional shares from the issuing company or from investors who have lent shares).

6. The Offer Price Setting Process

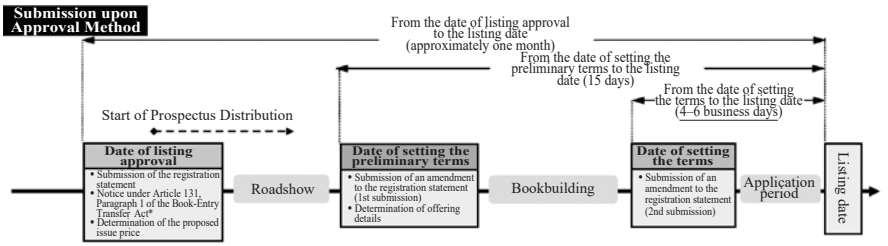
The offer price for an initial public offering (IPO) is generally set through filing a securities registration statement, assessing demand from institutional investors via a roadshow, setting preliminary terms, and assessing demand through bookbuilding.

In most IPOs, the issuing company submits the securities registration statement when approval for listing is given by the stock exchange (submission upon approval method). Under this method, the securities registration statement contains offer information such as the proposed issue price. The proposed issue price is the basis for the offer price. It is based on the theoretical price and other factors after discussions between the issuing company and the lead underwriter, and is provided as a guide to investment decisions. In addition, in order to incorporate the price expectations of institutional investors into the proposed issue price, the lead underwriter may conduct a demand survey before filing the securities registration statement.

In the roadshow, the issuing company presents its business and other key details to an audience primarily of institutional investors, and the lead underwriter conducts a demand survey, including the target purchase price and desired number of shares. The results of this survey will be used to determine the preliminary terms of the offer (usually a pricing range) to be indicated in the bookbuilding.

Next, the lead underwriter conducts a bookbuilding, in which it assesses general investor demand (including institutional investors) with respect to desired purchasing price and number of shares based on the preliminary terms. Subsequently, based on the results of its assessment, market conditions, and risks of price volatility ahead of the listing date, the issuing com-

Chart III-3. Illustration of the "Submission upon Approval" and "Pre-Approval Submission" Methods



*Notice regarding the issuing company's request to forward account notifications to existing shareholders

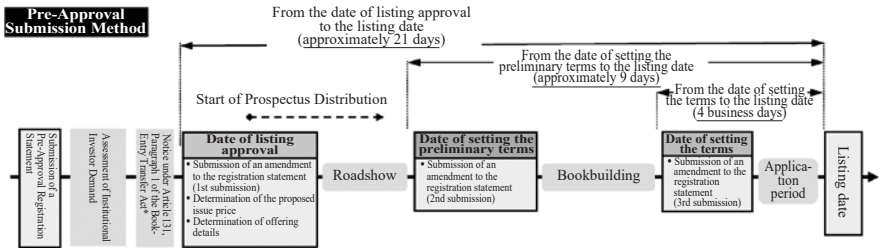


Table III-8. Certain range for setting the offer price outside the provisional price range and changing the number of shares offered

Summary of Changes, etc.	Within a Certain Range
• Setting the offer price outside the provisional price range • Changes to the number of shares offered	• Certain Range refers to cases where all of the following conditions (1) through (3) are met. (1) The offer price is determined within a range of not less than 80% of the lower limit of the preliminary terms and not more than 120% of the upper limit of the preliminary terms. (2) The number of shares to be sold at the time the offer price is set is within a range of not less than 80% and not more than 120% of the number of shares to be sold at the time the preliminary terms are set. (3) The offering size at the time the offer price is set (number of shares (sum of the number of shares offered and the number of shares sold) × offer price) must be within the range from the lower limit of the preliminary terms × the number of shares at the time the preliminary terms are set × 80% to the upper limit of the preliminary terms × the number of shares at the time the preliminary terms are set × 120%.

*Within a certain range, the above procedures may be followed without repeating the bookbuilding process.
*The securities registration statement and prospectus must state that the above changes may occur.

pany and lead underwriter discuss and determine the offer price. Provided that the required disclosures are made in the securities registration statement or other relevant documents, the offer price may, within prescribed limits, be set outside the preliminary terms, and the number of shares offered may also be changed, without the need to conduct a new round of bookbuilding.

Alternatively, issuing companies may submit a securities registration statement (which generally indicates that details such as the proposed issue price are not determined, but includes a provisional listing date) prior to receiving listing approval from the stock exchange (pre-approval submission method). The basic process is the same as the submission upon approval method. However, under this method, a securities registration statement is submitted prior to listing approval and prospective demand among institutional investors is assessed prior to listing approval. This shortens the period between listing approval and the actual listing date, generally allowing the proposed issue price to be determined with less exposure to price fluctuations. On the other hand, since issuing companies must file amended securities registration statements more frequently than under the submission upon approval method, additional costs for disclosure are involved.

7. Private Equity Market

Public offerings and other equity financing initiatives that raise capital from the general public are mostly conducted by public companies whose shares are traded on an exchange or other public market. However, that does not mean that private companies have to deal with particular legal restrictions in equity financing. In fact, equity financing regulations for private companies can be said to be more relaxed than for public companies. For example, there is no requirement to include information on the issuer's operating performance or financial position in the written notice of securities because, unlike the securities registration statement, this is not a disclosure of detailed information to investors. Furthermore, under the Financial Instruments and Exchange Act and other Cabinet Office Orders currently in force, if the proceeds from a proposed offering or secondary distribution of shares (securities) are less than ¥100 million, private companies are exempt from filing a securities registration statement. Instead the requirement is simply for a written notice of securities to be filed, regardless of whether or not there is solicitation of 50 or more people. In principle, if the proceeds from the offering are ¥10 million or less, or fewer than 50 persons are solicited, the issuer is not even obliged to file a written notice of securities. However, when viewed from the standpoint of investors, private equity investments, given the limitations on information available to them, involve higher risks. While

Table III-9. Criteria for Requirement to Submit Securities Registration Statement or Written Notice of Securities Under the Financial Instruments and Exchange Act, and Cabinet Office Order, etc.

		No. of Investors*1, 2	
		Less than 50	50 or more
Issue Amount	100 million yen or more*3	Not necessary	Securities Registration Statement
	10 million yen or greater but less than 100 million yen	Not necessary	Written Notice of Securities
	10 million yen or less	Not necessary	

Notes: 1. Under the current FIEA and Cabinet Office Orders, etc., even when the number of persons solicited is less than 50, if, for example, the total number of persons solicited for the same type of securities issued within the past six months is 50 or more, whether a securities registration statement or written notice of securities is required is determined based on the total issue price.

2. In accordance with the revision of Cabinet Orders effective April 1, 2003, issuance regulations were relaxed as follows.
   (1) Under certain conditions, such as the number of Qualified Institutional Investors being 250 or less, the number of professional securities investors, i.e., Qualified Institutional Investors, may be excluded from the count of 50 persons solicited.
   (2) Equity-related products, such as shares, were added to the scope of so-called "professional private placements," meaning solicitations for applications to acquire securities made only to Qualified Institutional Investors where there is little risk of transfer to persons other than Qualified Institutional Investors. In this case, regardless of the number of investors, a written notice of securities is required only for issues of ¥100 million or more (for cases involving fewer than 50 persons, see Note 1 above).

3. Consideration is being given to amending the FIEA in 2026 to raise the ¥100 million-or-more threshold, which triggers the requirement to file a securities registration statement for offers to 50 or more investors, to ¥500 million or more.

stock prices of public companies are properly formed through market transactions, reasonable values of private stocks are not easy to determine since there are various methods to estimate private stock prices, including the net asset method of estimating based on the company's net assets, the income method based on cash flows, and the dividend discount method based on future dividend projections. Moreover, the problem with private equity investments is the difficulty of recovering invested funds due to lack of liquidity. It is hard to recover funds until the investee company goes public. Thus investment in private equity tends to be limited to a small number of investors, such as venture capital funds, which have the economic capacity to tolerate the high risk and long investment periods associated with such investments. In order to stimulate entrepreneurial activity and foster startup businesses, streamlining the fund raising mechanism prior to going public has been dis-

Table III-10. Examples of methods of calculating stock values of private companies

1. Net assets approach
(1) Book value method Price per share = Book value of net assets/Total number of issued shares (2) Adjusted book value method Price per share = Book value of net assets reflecting unrealized gain and losses/Total number of issued shares (3) Market value method Price per share = Market value of net assets/Total number of issued shares
2. Income approach
(1) Income capitalization method (direct return method) Price per share = (Projected future net profit after tax/Capitalization ratio)/Total number of issued shares (2) DCF method Price per share = Total amount of discounted present value of projected future profit/Total number of issued shares
3. Dividend discount approach
(1) Dividend discount method Price per share = (Projected future annual dividends/Capitalization ratio)/Total number of issued shares (2) Gordon Growth Model method Price per share = (Projected future annual dividends/(Capitalization ratio-Investment return ratio × Retained ratio)

cussed as a matter of priority. The Japan Securities Dealers Association launched a public quotation system (Green Sheet system) for private equity and unlisted shares in July 1997. Securities companies became eligible to solicit investment in private equities for issues of OTC securities that met certain standards of information disclosure and for which the securities companies provide publicly announced buy and sell quotes. This system was succeeded by the Shareholders Community System, which was launched in May 2015. In July 2022, the J-Ships system was introduced to allow unlisted stocks and other securities to be issued and distributed to specified investors through securities companies. In addition, under the equity investment crowdfunding system, which was launched in May 2015, the investment cap of ¥500,000 for specified investors (professional investors) was abolished following the 2022 amendments to the Enforcement Order of the Financial Instruments and Exchange Act and the Cabinet Office Ordinance on Financial Instruments Business. In addition, raising the current cap on the aggregate issuance amount from less than ¥100 million is also under consideration.