DEREGULATION : COMPANY LAW AND ACCOUNTING FOR CAPITAL STOCK IN JAPAN

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• The views expressed in this presentation are those of the author. They are not official positions of the Japan Accounting Association.
PRESENTATION OUTLINE

1. Amount of minimum capital
2. Treasury stocks
3. Stock options
4. Surplus available for dividend
5. Many other issues
AMOUNT OF MINIMUM CAPITAL

1990 Commercial Code
- 10 million yen for Stock Company
- 3 million yen for Limited Liability Company

1999 Act for the Promotion of the Creation of New Businesses
- Exempt designated newly organized companies from the application of article 166-4 for 5 years

2005 Companies Act
- No minimum capital requirement
TREASURY STOCK

• Before the amendment of Commercial Code in 2004, to purchase treasury stock was prohibited except for the following four reasons

1. To cancel stocks by the original statute
2. Result of merger or purchase of business
3. To execute the right of the company
4. To exercise the redemption right of the company
AMENDMENT OF COMMERCIAL CODE & SPECIAL ACT

Amendment of the Commercial Code (purpose)
- To cancel
- For stock based payment

Special Act (to increase the available surplus)
- Land revaluation reserves
- Legal reserves
Before the Amendment of Commercial Code in 2004, treasury stocks were rare.

**Regulation on Accounts of Stock Company**
- Article 12 (1963) Treasury stock shall be listed in the Current Assets section separated from other stocks.
- Article 12 (2) (1982) Above clause shall be applied for the stock of the parent company.
AMENDMENT OF COMMERCIAL CODE

• 1994
  – For Employee Stock Ownership program
  – By approval at the stockholders’ meeting

• 1997
  – For treasury stock type stock options
LEGAL RESERVE

• **Legal Reserve**
  - not available for dividend
  - only for bonus stock

• **Special Act to Reacquire Capital Stock (1998)**
  Capital Reserve was made available for purchasing treasury stocks
LAND REVALUATION RESERVE

• Special Act for Land Revaluation (1999)
  Two third of the amount of Land Revaluation Reserve was made available for purchasing treasury stocks
AMENDMENT OF COMMERCIAL CODE

• 2001 June
• Amendment not proposed by the Cabinet
• As a principle, company may purchase treasury stock
  • The amount available for purchasing treasury stocks = amount available for dividend
• Procedure to reduce Legal Reserve for increasing surplus available for dividend
ACCOUNTING FOR TREASURY STOCK

• Treasury stock
  – Balance sheet
    Assets Section → Capital Section
    (deduction before capital total)

  – Income Statement
    Profit and Loss → Capital transaction
    (increase or decrease of other capital surplus)
COMPANIES ACT

• Section 4 Acquisition of Own Shares by Stock Company
  – Article 155 A Stock Company may acquire shares issued by such Stock Company only in the following cases:
  – Article 156 (1) A Stock Company shall prescribe the following matters by resolution of a shareholders meeting in advance in order to acquire for value own shares by agreement with its shareholders; provided, however, that the period under item (iii) cannot exceed one year:

http://www.japaneselawtranslation.go.jp/law/detail/?id=2035&vm=04&re=01&new=1
STOCK OPTIONS IN JAPAN

• 1980s U.S. companies granted stock options directly to the officers of the subsidiaries in Japan
• 1995 Quasi-stock options by SONY using detachable stock purchase warrants
• 1995 Quasi-stock options by SOFTBANK using principal stockholder’s stocks
STOCK OPTIONS IN COMMERCIAL CODE

• Amendment of New Business Promotion Act in 1995
  – Only for designated venture firms

• Amendment of Commercial Code in 1997
  – Treasury stock type
  – Stock purchase right type
    • Only for employees and directors of the company
    • Not for subsidiaries’
ACCOUNTING STANDARD FOR STOCK OPTIONS

• 2005
  – ASBJ Statement No. 8 Accounting Standard for Share-based Payment
  – ASBJ Guidance No. 11 Guidance on Accounting Standard for Share-based Payment

• Forfeiture of *vested* stock options results in recognizing gain
STOCK OPTIONS IN COMPANIES ACT

• Chapter III Share Option
  – Section 1 General Provisions
    • Article 236 (1) If a Stock Company issues Share Options, the features of the Share Options shall consist of the following matters:

• Allowed to grant stock options
  – to any person
  – for any amount
  – for any purpose
    • Article 309 (2) As long as approved by the resolutions of the shareholders meetings made by a majority of two thirds (Article 240 (1) in case of Public Company, “shareholders meeting” shall be read as “board of directors meeting.”)
DIVIDENDS OF SURPLUS

• Chapter V Accounting
  – Section 1 Accounting Principle
    • Article 431  The accounting for a Stock Company shall be subject to the business accounting practices generally accepted as fair and appropriate.
    • Article 446 (Amounts of Surplus)
  – Section 4 Dividends of Surplus
    • Article 453  A Stock Company may distribute dividends of surplus to its shareholders (excluding such Stock Company).
AMOUNT OF SURPLUS

• Article 446 The amount of the surplus of a Stock Company shall be the amount obtained by subtracting the sum of the amounts listed in item (v) through (vii) from the sum of the amounts listed in item (i) through (iv):
  - (i) The amount obtained by subtracting the sum of the amounts listed in Sub-item (c) through (e) from the sum of the amounts listed in Sub-item (a) through (b) as at the last day of the Most Recent Business Year:
    (a) The amount of assets;
    (b) The sum of the book value of Treasury Shares;
    (c) The amount of debt;
    (d) The sum of the amount of stated capital and Reserves;
    (e) The sum of the amounts, other than those listed in Sub-item (c) and (d), recorded in each account title prescribed by the applicable Ordinance of the Ministry of Justice.
ORDINANCE OF THE MINISTRY OF JUSTICE

- Part 7 Chapter 1 Amount of surplus of stock company
  - Article 149
  - Article 150

- Chapter 6 Amount available for distribution
  - Article 156
  - Article 157
  - Article 158
MANY OTHER ISSUES

• Internal Control
• Sustainability Reporting
• Accounting Schools