Foreign Exchange and Foreign Trade Act Foreign Investment Screening System

Annual Report (FY2023)





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1. Foreword

As four years have passed since the implementation of the foreign investment screening system under the 2019 revised Foreign Exchange and Foreign Trade Act (hereinafter referred to as "FEFTA"), we have decided henceforth to publish an annual report on the investment screening system.

FEFTA is a law that governs cross-border financial flows. Amid recent changes in the environment surrounding economic security, it has become important to ensure a balance between (1) the need to further promote investment in Japan that contributes to sound economic development under the principle of freedom of transactions and (2) responding to economic security requirements. As the Government of Japan currently aims to maintain Japan's position as an international financial center open to the world, we believe that appropriate measures through the effective enforcement of the investment screening system against investments that may impair national security will also contribute to the promotion of sound economic activities and the development of sound markets. It is important to carefully design this system with an eye on both regulations and the market.

This annual report also publishes various statistical data related to the foreign investment screening system along with comprehensively explaining the system and its history, the authorities' views on screening and monitoring, and system management practices. In particular, the report summarizes recent policy trends, such as the enhancement of the screening and monitoring regime and the authorities' efforts to detect non-notified cases. The annual report also illustrates in detail the various stages and decision points in the foreign investment screening system, in addition to outlining the Government's policy on promoting investment in Japan and policy trends related to economic security.

We hope that this annual report will help to improve the transparency of the FEFTA foreign investment screening system for all investors and to promote dissemination of this vital policy for Japan's economy.

Atsushi MIMURA

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Ministry of Finance

2. Outline of the system (general explanation)

(1) Outline of FEFTA

FEFTA provides for fundamental matters on foreign transactions (cross-border payments and various transactions). Article 1 of the Act states, "The purpose of this Act is to, based on freedom of foreign transactions, such as foreign exchange and foreign trade, ensure the normal development of foreign transactions and the maintenance of peace and security in Japan or international society by conducting the minimum necessary control or coordination of foreign transactions, thereby bringing about a balance of payments equilibrium and stability of currencies and contributing to the sound development of the Japanese economy."

Under FEFTA at the time of its enactment (1949), foreign transactions were prohibited in principle due to the centralized management of foreign currencies and the reconstruction of domestic industry after the war. After gradual liberalization, however, the current FEFTA now serves as a framework for free foreign transactions in principle (see "Column 1"). It also functions as a law to implement measures such as asset freezing for economic sanctions and the prevention of international financial system abuse, and as a tool to control foreign transactions for security purposes and in dealing with economic emergencies. Data requested under FEFTA are used to prepare balance of payments statistics and understand market trends.

Overview of FEFTA (Foreign Exchange and Foreign Trade Act)

Points

- > FEFTA provides for fundamental matters on foreign transactions (cross-border payments and various transactions)
- When FEFTA was first enacted (1949), foreign transactions were prohibited in principle in order to centralize the management of foreign currency and rebuild domestic industry, but liberalisation of the framework has since progressed step by step, and foreign transactions are in-principle free under the current framework.
- > The Act also functions to implement measures such as economic sanctions and other measures to freeze assets to prevent abuses of the international financial system.
- > It also serves as a tool for controlling foreign transactions for security purposes and in dealing with economic contingencies.
- > Data collected under FEFTA is also used to compile balance of payments statistics and to monitor market trends.

Purpose of FEFTA (Article 1)

The purpose of this Act is to, <u>based on freedom of foreign transactions</u>, such as foreign exchange and foreign trade, ensure the normal development of foreign transactions and the maintenance of peace and security in Japan or international society by conducting the <u>minimum necessary control or coordination</u> of foreign transactions, thereby bringing about a balance of payments equilibrium and stability of currencies and contributing to the sound development of the Japanese economy.

- O Principle: freedom of foreign transactions
- **Exceptions:** minimum necessary control or coordination → Restrictions may apply to foreign transactions

<u>①economic sanctions</u>: Blocking of funds and freezing of assets related to terrorism, development of nuclear weapons

in breach of international commitments, etc.

 $\underline{@investment\ restrictions}:\ Certain\ restrictions\ on\ acquisitions\ of\ certain\ business\ sectors\ by\ foreign\ capital\ such\ as$

defense industry, nuclear power, water supply, railways and software

<u>③economic emergency</u>: In the case of rapid fluctuations in foreign exchange markets and sudden capital flows that have a negative impact on the macroeconomy

(2) Outline of the Foreign Investment Screening System

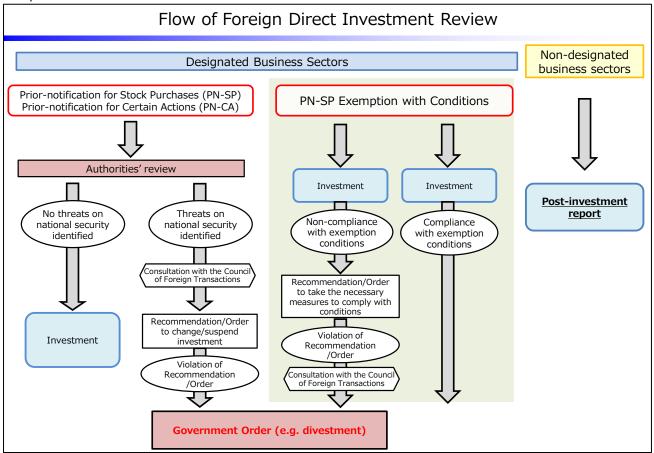
FEFTA requires prior notification for certain types of foreign investors' transactions and actions, such as inward direct investment, in certain cases from the viewpoint of ensuring national security, maintaining public order, protecting public safety, and ensuring the smooth operation of the Japanese economy, while maintaining the principle of freedom of foreign transactions. The Minister of Finance and the ministers in charge of relevant business sectors are prescribed to screen the notification (FEFTA Article 27: Screening of prior notification for inward direct investment and equivalent actions). In addition, before a foreign investor acquires shares or equity in an unlisted company in Japan through a transfer from another foreign investor, prior notification is also required and screened from the viewpoint of ensuring national security (FEFTA Article 28: Screening of prior notification for specified acquisitions).

As shown in the figure below, the investment screening system under FEFTA can be roughly classified into three types.

First, the left hand side covers investment in business sectors designated from the viewpoint of national security, etc. (designated business sectors in (5) below) for which prior notification is required in principle. The Ministry of Finance and other ministries responsible for relevant business sectors screen the notification to see if the investment in question impairs national security or is inconsistent with the other objectives under FEFTA as earlier stated. If the screening finds it does, the authorities may recommend or order the modification or discontinuance of the investment in question after taking the prescribed procedures, such as hearing opinions from the Council on Customs, Tariff, Foreign Exchange and Other Transactions (hereinafter referred to as the "Council on Foreign Transactions") (FEFTA Article 27). If the relevant foreign investor violates the recommendation or order, the authorities may order necessary measures, such as the disposal of shares (hereinafter referred to as "order for measures") (FEFTA Article 29). With regard to FEFTA Article 27, the authorities have recommended and ordered a foreign investor to cancel the acquisition of shares in a Japanese electric power-related company in the past, taking into account the impact of the acquisition on the management of the company (the impact was judged comprehensively based on circumstances such as the foreign investor's investment policy and activities) and the risk of hindering the maintenance of public order (the risk of affecting Japan's policy of a stable electricity supply was identified).

Second, the middle of the figure covers investment for which the prior notification exemption system can be used. Only if a foreign investor complies with the exemption conditions, such as refraining from being involved in the management of the target company and from accessing secret non-public technology information, and can demonstrate that the investment is considered to be purely for the purpose of asset management, the investor may be exempted from the prior notification obligation but are required to submit the post investment report after its implementation. If the foreign investor violates the exemption conditions, however, the authorities may recommend or order the investor to take necessary measures to comply with the conditions (FEFTA Article 27-2). If the foreign investor violates the recommendation or order, the authorities may order necessary measures, such as the disposal of shares after taking the prescribed procedures, such as hearing opinions from the Council on Foreign Transactions, in the same way as the first case outlined in the preceding paragraph (FEFTA Article 29).

Lastly, the right hand side covers investment in non-designated business sectors, for which a post investment report is required.



< Column 1> History of the Foreign Investment Screening System of Japan

Japan's inward direct investment system started with the Foreign Capital Act (hereinafter referred to as the "defunct Foreign Capital Act") enacted in 1950 as a special law for the then FEFTA. Reflecting the economic situation just after the war, the defunct Foreign Capital Act, unlike the current FEFTA, aimed to "permit the investment of foreign capital that contributes to the independence and sound development of the Japanese economy and the improvement of the balance of payments, secure remittances arising from the investment of foreign capital, take appropriate measures for protecting such foreign capital, and thereby create a sound basis for the investment of foreign capital in Japan." As Japan's foreign exchange situation was extremely unstable then, overseas remittances accompanying foreign economic transactions were strictly regulated by the then FEFTA in general. On the other hand, the defunct Foreign Capital Act required the introduction of foreign capital to be approved by the competent minister in principle and guaranteed remittances for approved transactions for the purpose of selectively introducing high-quality foreign capital to protect the balance of payments, reflecting the state of the Japanese economy undergoing reconstruction.

As Japan gradually improved its position in the international economy becoming an industrialized country in the second half of the 1960s, this closed policy was reviewed from the perspective of Japanese economic development and the promotion of international cooperation. Subsequently, the regulations under the then FEFTA and the defunct Foreign Capital Act were successively relaxed for the liberalization of capital. After Japan's accession to the Organization for Economic Cooperation and Development (OECD) in 1964 it was obliged to gradually eliminate restrictions on capital movements in accordance with the OECD Code of Liberalization of Capital Movements. This included specific liberalization measures to expand the scope of business sectors for liberalization from 1967 to 1973. Subsequently, the defunct Foreign Capital Act was abolished in 1979 in a manner to be integrated into the then FEFTA. The foreign investment approval system (prohibition in principle) was then replaced by the reporting system (liberalization in principle) to promote the institutional liberalization of foreign investment.

As capital flows between Japan and other countries grew briskly in line with Japan's growing weight in the world economy from 1985 to 1989, Japan's overseas direct investment noticeably increased while foreign direct investment in Japan, though growing, slipped below the amount of Japan's overseas investment. Against this backdrop, Japan and the United States discussed their external direct investment policies at their Structural Impediments Initiative talks. The Japanese Government accordingly offered to consider revising the then FEFTA. In response, the FEFTA revision in 1991 replaced the in-principle prior notification system with the in-principle ex post facto reporting system regarding the screening of foreign investment under FEFTA, while maintaining the prior notification requirement for some business sectors. Regulations on foreign investment were thus liberalized further. Specifically, the revision switched from prior notification subject to same-day processing to ex post facto reporting for most business sectors, simplifying relevant procedures significantly. (Until the 1991 revision, prior notification was required for all business sectors in principle while a 30-day prohibition was established on any investment deal. In practice, however, prior notification for business sectors that clearly did not fall under the category of national security-related sectors were processed on the same day, allowing investors to implement the relevant investment transactions on the same day of the prior notification.) Later, business sectors which require prior notification were updated when necessary. When the then FEFTA was revised into the current FEFTA for full foreign exchange liberalization in 1998, the word "control" was deleted from the name of the act.

Subsequent major FEFTA revisions in 2017 included the introduction of Specified Acquisition, a new category of transaction that requires prior notification for screening (FEFTA Article 28) and a new clause for orders for measures against non-notified cases, false notification, and the violation of orders to modify or discontinue relevant transactions (FEFTA Article 29. (2) above). The 2019 revision enhanced regulations regarding national security by lowering the threshold stake for the acquisition of listed shares from 10% to 1% and establishing prior notification for Certain Actions, while easing regulations by introducing the prior notification exemption system. This revision established a basic framework for the screening of foreign investment under the current FEFTA. Subsequently, the revisions of designated business sectors were taken in line with economic security requirements.

(3) Types of Foreign Investors Subject to the Screening System

Foreign investors subject to the foreign investment screening system are defined in Article 26, Paragraph 1 of FEFTA as those who implement inward direct investment and equivalent actions, or specified acquisitions, as follows. In this respect, individuals are defined with a focus on residency. Even Japanese nationals are considered foreign investors subject to the foreign investment screening system if they reside abroad. On the other hand, foreign nationals who do not have Japanese nationality are not subject to this system if they are residents of Japan. As for corporations, even companies and partnerships established in Japan may fall under foreign investors in certain cases (so-called "resident foreign investors") as described in items (iii) to (v) below:

- (i): An individual who is a non-resident
- (ii): A juridical person or other organization established pursuant to foreign laws and regulations
- (iii): A (Japanese) corporation for which a majority of voting rights are held by items (i) and (ii)
- (iv): A partnership that is owned 50% or more by items (i) and (ii) and a partnership for which items (i) and (ii) account for a majority of operating partners.
- (v): A corporation or any other organization for which non-resident individuals account for a majority of directors or holders of representation rights.

(4) Types of Foreign Direct Investment and Equivalent Actions Subject to the Screening System

Actions subject to the foreign investment screening system, including the acquisition of shares, are defined in Article 26, Paragraph 2 of FEFTA as follows: In addition to the acquisition of shares, consent to substantial changes in the purpose of business, appointments to directors, etc., transfer or abolition of all or a part of business operations (item v), the establishment of a branch office (item vi), and loans to domestic corporations of more than one year (when the balance exceeds 100 million yen or more than 50% of liabilities) (item vii) are defined as types of inward direct investment subject to prior notification and screening.

- (i): Acquisition of shares or equity in an unlisted company
- (ii): Transfer of shares or equity in an unlisted company by a non-resident who was formerly a resident
- (iii): Acquisition of 1% or more of the total outstanding shares of a listed company
- (iv): Acquisition of 1% or more of the total voting rights of a listed company
- ■(v): Consent to substantial changes in the business purpose of the company and other matters that have a significant impact on the management of the company (e.g., appointments of directors or transfer of important business operations)
- (vi): Establishment of branches, etc., or substantial changes in the type or business purpose of branches, etc.
- (vii): Money loans of more than one year
- (viii): Acquisition of business operations, etc.
- ■(ix): Actions stipulated by Cabinet Order as actions equivalent to the preceding ones (stipulated in Article 2, Paragraph 16 of the Cabinet Order on Inward Direct Investment)

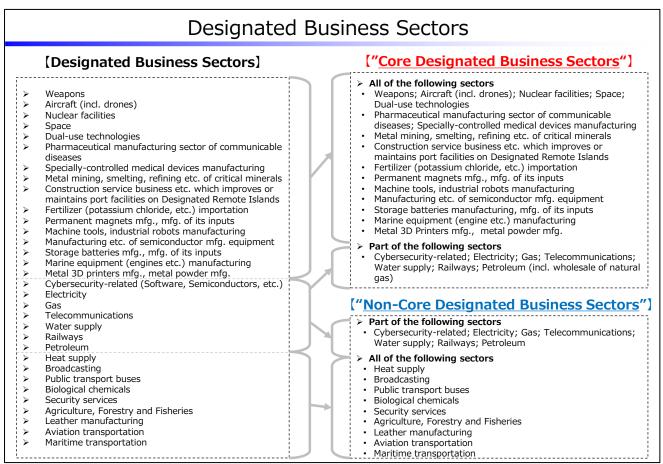
(5) Designated Business Sectors

Under the principle of free foreign transactions, the foreign investment screening system designates business sectors for inward direct investment by foreign investors subject to prior notification in certain cases from the perspective of national security and other aforementioned objectives under FEFTA.

The designated business sectors include core sectors selected for detailed screening from the viewpoint of national security and other objectives. In principle, the prior notification exemption system cannot be used for such core business sectors. However, if certain foreign financial institutions acquire shares in listed companies, etc. and comply with exemption conditions (blanket exemption) or if other foreign investors acquire less than 10% of shares in listed companies, etc. and comply with two additional exemption conditions (exemption conditions on core sectors' business activities) (regular exemption), the prior notification exemption system can be used.

^{*} When an equity stake is calculated, a foreign investor's stake is added to those of a closely related person of the investor.

Core and other designated business sectors are stipulated in Public Notices by the Ministry of Finance and other ministries responsible for relevant business sectors and are constantly updated to reflect economic security requirements within the foreign investment screening system framework. Based on this policy, new core designated business sectors were added in May 2023 from the viewpoint of securing stable supply chains and addressing the risk of technology leakage and the military diversion of commercial technologies, in response to the designation in April 2023 of "specific critical products" subject to stable supply support under the Act on the Promotion of Ensuring National Security through Integrated Implementation of Economic Measures (hereinafter referred to as the "Economic Security Promotion Act"). The current core and other designated business sectors are as follows:



Note: The above are the designated business sectors after the amendment of the Public Notices in April 2023 and differ from the latest list.

<Column 2> Recent Policy Responses to Economic Security

Reflecting a more complex international environment and changing socio-economic structures, forestalling acts that harm the security of the state and its people in relation to economic activities have become increasingly important for ensuring national security. To this end it is necessary to comprehensively and effectively promote economic measures that also ensure national security. Accordingly, Japan enacted the Economic Security Promotion Act in May 2022. In order to respond to urgent issues, the act created four systems: (1) a system to ensure the stable supply of critical products, (2) a system to ensure the stable provision of essential infrastructure services, (3) a system to support the development of advanced critical technologies, and (4) a system to ensure the non-disclosure of patent applications. Specifically:

- (1) The system ensures the stable supply of products that have a significant impact on the survival of the people and on the national life and economy.
- (2) The system is required to prevent important facilities of essential infrastructure from being used to interfere with the stable provision of essential infrastructure services (electricity, gas, water, etc.) that are significant for national security.
- (3) The system is necessary for proving financial and public-private support for the development of cutting-edge critical technologies that could be used in the future not only for the private sector but also in various fields, such as government infrastructure, measures against terrorism and cyberattacks, and national security, as the promotion of their research and development and their appropriate utilization are required to continuously ensure Japan's stability in the international community.
- (4) The system is important for reserving disclosure procedures for patents on inventions of which disclosure
 is likely to impair the security of the nation and its people and for preventing their sensitive disclosure and
 information leakage.

Various measures are implemented for these systems under the Economic Security Promotion Act.

Furthermore, the National Security Strategy revised in December 2022 explicitly called for "promoting economic security policies to achieve autonomous economic prosperity," implying that the government consider how to enhance the FEFTA foreign investment screening system for the purpose of fostering and preserving technologies.

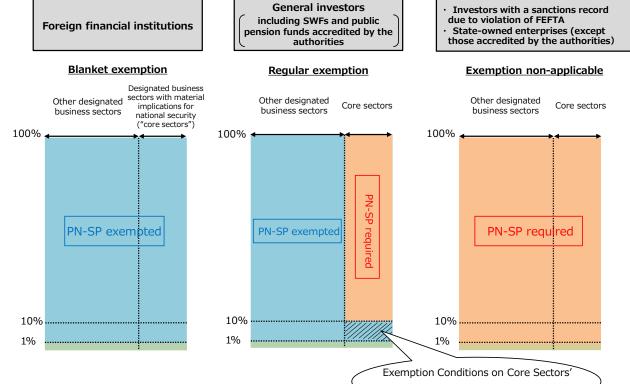
This series of government policy directions is one of the important guidelines for considering the appropriate FEFTA inward direct investment screening system. Considering such economic security requirements, it is important to review the foreign investment screening system in a timely and appropriate manner based on constant verification and consideration.

(6) Prior Notification Exemption System

Prior notification may not be required for the acquisition of shares and voting rights in listed companies, etc., and the acquisition of shares and equity in unlisted companies, etc. among inward direct investment transactions made by foreign investors, only if they comply with certain conditions (exemption conditions), such as refraining from being appointed as directors and accessing secret non-public technology information. However, foreign investors who have been punished for violating FEFTA in the past or state-owned enterprises or those controlled by state-owned enterprises cannot use the prior notification exemption system.

A foreign investor who has used the prior notification exemption system must submit to the authorities a post-investment report pledging to abide by the exemption conditions within 45 days after implementing a relevant investment transaction. If a foreign investor who has used the prior notification exemption system violates the exemption conditions, the authorities may recommend and order the investor to correct the violation. If the investor fails to abide by the recommendation and order, the authorities may order the investor to take measures such as the disposal of shares. Any foreign investor who refuses to abide by such order may be subjected to criminal punishment. The outline of the exemption conditions and the thresholds for the post-investment report for the use of the prior notification exemption system is as follows:

Exemption Scheme for Prior-notification of Stock Purchases (PN-SP) of listed companies General investors including SWFs and public including SWFs and public including SWFs and public



Exemption Scheme for Prior-notification for Stock Purchases of listed companies

Types of investors	Scope				
Foreign financial institutions	Designated business sectors other than core sectors	<"Blanket exemption"> • PN-SP will be exempted with no upper limit for investors that comply with the Exemption Conditions (a,b,c) • Post-investment report – from 10%			
General investors	Designated business sectors other than core sectors	<"Regular exemption"> PN-SP will be exempted with no upper limit for investors that comply with the Exemption Conditions (a,b,c) Post-investment report - from 1% 			
(including SWFs and public pension funds accredited by the authorities)	Core sectors	PN-SP will be exempted under 10% for investors that also comply with the Exemption Conditions on Core Sectors' Business Activities (d,e) Post-investment report - from 1%			
Investors with a sanctions record due to violation of FEFTA State-owned enterprises (except those accredited by the authorities)	Designated business sectors other than core sectors	No exemption is applicable			

[Exemption Conditions]

- a) Investors or their related persons will not become board members of the investee company.
- Investors will not propose to the general shareholders' meeting transfer or disposition of investee company's business activities in the designated business sectors.
- Investors will not access non-public information about the investee company's technology in relation with business activities in the designated business sectors.

[Exemption Conditions on Core Sectors' Business Activities]

Business Activities

- Regarding business activities in core sectors, investors will not attend the investee companies' executive board or committees that make important decisions in these activities.
- Regarding business activities in core sectors, investors will not make proposals, in a written form, to the executive board of the investee companies or board members requiring their responses and/or actions by certain deadlines.

Exemption Scheme for Prior-notification for Stock Purchases of unlisted companies

Types of investors	Scope				
Foreign financial institutionsGeneral investors	Designated business sectors <u>other than</u> core sectors	 PN-SP will be exempted with no upper limit for investors that comply with the Exemption Conditions (a,b,c) Post-investment report is necessary 			
(including SWFs and public pension funds accredited by the authorities)	Core sectors	·No exemption is applicable			
Investors with a sanctions record due to violation of FEFTA State-owned enterprises (except those accredited by the authorities)	Designated business sectors other than core sectors	·No exemption is applicable			

[Exemption Conditions]

- a) Investors or their related persons will not become board members of the investee company.
- b) Investors will not propose to the general shareholders' meeting transfer or disposition of investee company's business activities in the designated business sectors.
- c) Investors will not access non-public information about the investee company's technology in relation with business activities in the designated business sectors.

<Column 3> Types of Foreign Investors and Investment Transactions That Cannot Use the Prior Notification Exemption System

In principle, the prior notification exemption system cannot be used if foreign investors fall under the following categories of foreign investors or conduct specific investment transactions, such as those who have been punished for violating FEFTA in the past or state-owned enterprises or those controlled by state-owned enterprises.

[Types of foreign investors who cannot use the prior notification exemption system]

- Those who have completed a term of criminal punishment for violation of FEFTA or violated administrative orders under FEFTA within the past five years
- Those who have been ordered to take measures in the past for violating the exemption conditions
- Foreign governments, etc. and companies controlled by foreign governments, etc. (excluding accredited sovereign wealth funds (SWFs), etc.)

[Types of investment transactions that cannot use the prior notification exemption system]

- Investment in business sectors designated in Public Notices for detailed screening from the viewpoint of national security, etc. (core business sectors)
 (However, if certain foreign financial institutions comply with the exemption conditions when acquiring shares in listed companies, etc. (blanket exemption) and if regular investors comply with exemption conditions on core sectors' business activities when acquiring less than 10% of shares in listed companies, the prior notification exemption system can be used.
- Investment transactions that aim to make it difficult for business operations in designated business sectors to be conducted continuously and stably
- Investment transactions that have the purpose of committing actions that are contrary to complying with the exemption conditions

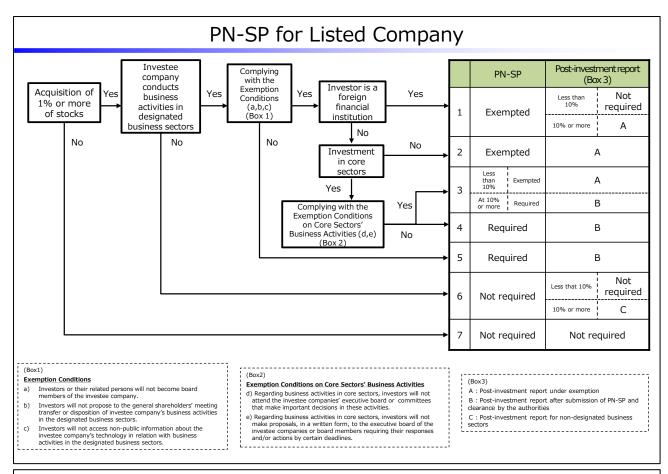
"Investment transactions that aim to make it difficult for business operations in designated business sectors to be conducted continuously and stably" among the above "types of investment transactions that cannot use the prior notification exemption system" are defined in Article 3-2, Paragraph 2, Item 4 of the Cabinet Order. If an inward direct investment transaction that can use the prior notification exemption system is accompanied by an action to endanger the survival of business operations for any of designated business sectors, the transaction may not be subject to the prior notification exemption system because the premise for allowing prior exemption is not valid. Whether or not this applies may be determined depending on the specific circumstances of each case, such as the nature of business operations, the manner of the relevant investors' conduct, and the impact of the conduct expected by the investor on the implementation of business operations. In a case in which an investment transaction is subject to this item, a prior notification may allow the authorities to recommend the relevant investor to revise or cancel the transaction. For example, this item may cover a case in which a foreign investor acquires substantial shares in a company for the purpose of making a proposal leading to the downsizing of business operations that are required to be implemented continuously and stably from the viewpoint of national security, etc., thus indicating that the investor's influence accompanying the share acquisition may compel the company to have no choice but to realize the investor's proposal.

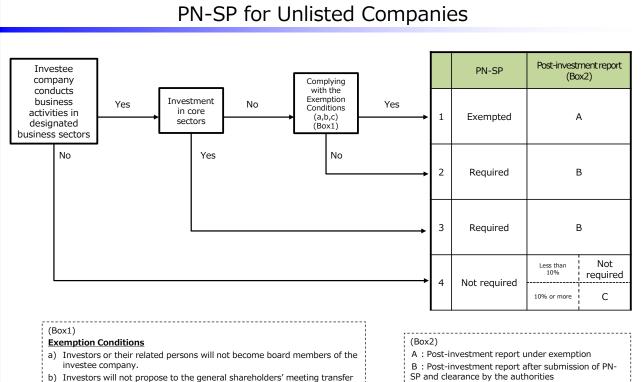
As for "investment transactions that have the purpose of committing actions that are contrary to complying with the exemption conditions," Order on Inward Direct Investment delegated from Article 3-2, Paragraph 2, Item 5 of the Cabinet Order stipulates the following investment transactions as those indicating that investors have no willingness to comply with the exemption conditions: an inward direct investment transaction for a foreign investor who aims to become a director or auditor of a target company, and an inward direct investment transaction for a foreign investor who aims to propose a business transfer at a general meeting of shareholders at a target company. The stipulation means that as long as foreign investors comply with the exemption conditions and exemption conditions on core sectors' business activities, they are considered to be able to ensure national security in the same way as if prior notification is made. "Investment transactions that have the purpose of committing actions that are contrary to complying with the exemption conditions" are not qualified to use the prior notification exemption system because such transactions are recognized as likely to lead to the risk of harming national security, etc.

The prior notification exemption system was introduced through the FEFTA revision in 2019 from the perspective of further promoting inward direct investment that leads to the sound development of the economy and is an important system from the perspective of securing open markets. Meanwhile considering the current situation surrounding economic security, it is important to take appropriate measures against investment transactions that may damage national security, etc. It is important for the authorities to strive for the appropriate operation and enforcement of the foreign investment screening system, including the prior notification exemption system, by taking strict measures against cases that may fall under this item.

(7) Flowchart of Prior Notification of Stock Acquisition, Certain Actions (listed, unlisted, investment funds)

There are several types of prior notification and post-investment report requirements related to the foreign investment screening system under FEFTA, depending on specific actions, etc. A flowchart of such notification is as follows:





C: Post-investment report for non-designated

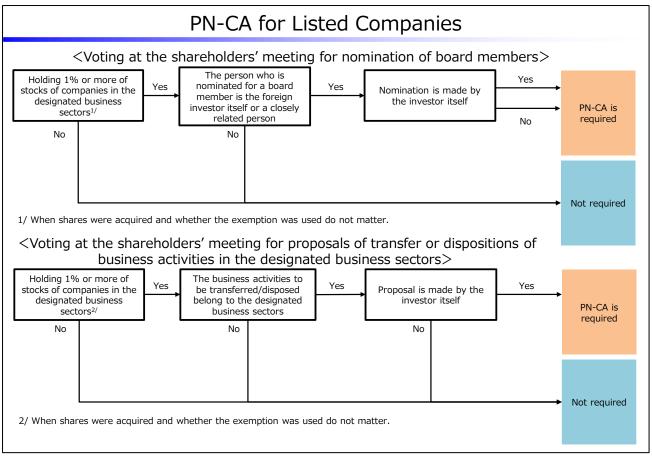
business sectors

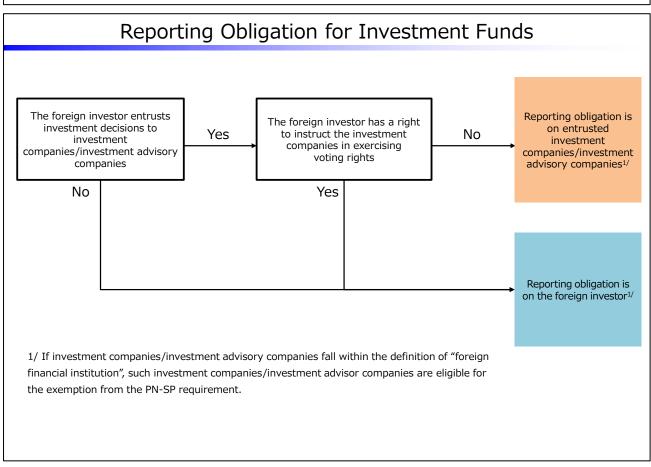
or disposition of investee company's business activities in the designated

Investors will not access non-public information about the investee company's technology in relation with business activities in the

business sectors.

designated business sectors.





Column 4> Initiatives to Promote Investment in Japan and Status of Investment in Japan

As sound inward direct investment plays an important role in the development of the Japanese economy, the further promotion of such investment is an important policy issue. The "Basic Policy on Economic and Fiscal Management and Reform 2023: Accelerating New Form of Capitalism -- Expanding Investment for the Future and Realizing Structural Wage Increases (Basic Policy 2023)," which was approved by the Cabinet in June 2023, stated: "It is also important to expand investment in Japan as a whole by actively attracting people, goods, money, and ideas from overseas, thereby enhancing innovation to further economic growth in our country. Aiming to achieve the target of 100 trillion yen in inward foreign direct investment by 2030..., the Government will implement the 'Action Plan for Attracting Human and Financial Resources from Overseas'..., thereby leading to sustainable growth of the national economy and revitalization of regional economies."

The balance of inward foreign direct investment in Japan, though having increased more than 2.5-fold from 19.6 trillion yen at the end of 2013 to 50.5 trillion yen at the end of 2023, has fallen far short of achieving the 2030 target of 100 trillion yen. The Government will focus on various initiatives to achieve the target. Specifically, the "Action Plan for Attracting Human and Financial Resources from Overseas" formulated in May 2023 calls for securing the sustainable growth of the Japanese economy and the revitalization of regional economies by implementing a five-pillar plan: (1) Stimulating investment in strategic sectors and restructuring global supply chains in light of the changes in the international environment, (2) Strategies for the formation of Asia's largest startup hub, (3) Attracting highly skilled foreign professionals, and improving the system for establishing a center for global knowledge exchange, (4) Improving the business and living environment to attract human resources and investment from overseas, and (5) Fundamentally strengthening the all-Japan's system to attract investment and to follow-up this Action Plan, and globally disseminating these activities through the Group of Seven summit and other forums.

[Reference]

Cabinet Office website: "Invest Japan" https://www.cao.go.jp/invest-japan/en_index.html

3. Recent Developments in the Inward Direct Investment Screening System

(1) Developments in FY2023

As four years have passed since the enforcement of the revised FEFTA in 2019, the impact of the enforcement has generally stabilized. The number of prior notifications decreased slightly, from 2,859 in FY2021 to 2,426 in FY2022, but rose to a record 2,871 in FY2023, close to the FY2021 level. International comparisons indicate that Japan's foreign investment screening system features a far larger number of prior notifications due to the relatively wider range of business sectors subject to prior notification for screening (details are described later).

A breakdown of prior notifications by business sector shows that cybersecurity-related sectors continued to account for the largest share of the total notifications from FY2020, standing at 58% for FY2023, followed by 15% for infrastructure-related sectors and 12% for sectors related to weapons, aircraft, nuclear power, outer space, etc. A breakdown by nationality shows that the major countries are Japan, the United States, the Cayman Islands, Singapore, and Hong Kong. There was no major change in the order and the number of notifications. The reason why Japan is ranked first is that Japanese companies where a majority of voting rights are held by non-resident individuals and foreign companies are treated as foreign investors under FEFTA and such investors also file a large number of notifications.

In FY2023, the average screening period and the share for prior notifications for which screening was completed within two weeks remained almost unchanged from previous years, standing at 9.1 days and about 70%, respectively.

The number of prior notification withdrawals (see 4. (3) below) has been on an upward trend since FY2020, rising to 399, or 13.9% as a ratio to the number of notifications (the number of withdrawals is not included in the number of notifications).

The number of report requests (see 4. (4) below) was 1 in FY2023.

The number of non-notified cases (see 4. (7) below) increased from 133 in FY2021 to 238 in FY2023, due partly to the authorities' vigorous efforts to detect non-notified cases in recent years.

The number of foreign investment transactions using the prior notification exemption system (see 4. (8) below) was 629 in FY2023, compared with 960 in FY2020 after the introduction of the system.

There was no record of order for modification, discontinuance/ order for measures and penalties in FY2023.

In a change to the foreign investment screening system in FY2023, the Public Notices was amended to add new core designated business sectors from the viewpoint of securing stable supply chains and addressing the risk of technology leakage and the military diversion of commercial technologies in response to the designation in April 2023 of "specific critical products" subject to stable supply support under the Economic Security Promotion Act. In response to the change, the List of Classifications of Listed Companies regarding the Prior-notification Requirements on Inward Direct Investment was updated for publication on the Ministry of Finance website in May 2023.

(2) Enhancement of the Screening and Monitoring Regime

Since the FEFTA revision in 2019, the authorities have been trying to enhance the screening and monitoring regime for the foreign investment screening system. Specifically, the Ministry of Finance established the Foreign Investment Policy and Review Office in 2020. Regarding economic security and the FEFTA foreign investment screening system, the "Basic Policy on Economic and Fiscal Management and Reform 2022: For a New Form of Capitalism -- Achieving a Sustainable Economy by Harnessing Processes to Overcome Challenges to Drive Growth (Basic Policy 2022)" stated that "the Government will enhance information collection, analysis, monitoring, etc., including at local finance bureaus," "seek to strengthen its organizational structure for promoting economic security together with relevant ministries and agencies," and "enhance the necessary capacity for collecting and analyzing intelligence to buttress our intelligence capabilities." This policy was maintained in the "Basic Policy on Economic and Fiscal Management

and Reform 2023: Accelerating New Form of Capitalism -- Expanding Investment for the Future and Realizing Structural Wage Increases (Basic Policy 2023)." Based on this policy, the Local Finance Bureaus, which are regional branches of the Ministry of Finance, have appointed officials in charge of the foreign investment screening system since 2022 to disseminate information about the system by holding briefings on the system and to provide consultation and collect information by setting up contact points for tips and referrals. Given the environment surrounding economic security has become increasingly severe, it is important to collect and analyze information on movements of and investment in local companies with sensitive and important technologies. To this end, the Ministry of Finance has been utilizing the Local Finance Bureaus to collect and analyze such information in order to further strengthen the screening and monitoring regime.

The foreign investment screening system in Japan features a far lower threshold than its foreign counterpart systems for mandatory prior notification of foreign investment transactions to acquire voting shares in listed companies. All other G7 countries, excluding the United States, which has no such threshold and reviews foreign investment based on details of transactions, have set the threshold at 10% or more, against 1% in Japan. This is because Japan's Companies Act authorizes a person who holds 1% or more of voting shares in a company have the right to make proposals at the company's general shareholders meeting. Since Japan has a prior notification exemption system, all foreign direct investment transactions that acquire 1% or more of voting shares in Japanese companies are not necessarily subject to prior notification. However, Japan's foreign investment screening system has a relatively wider scope of investment transactions subject to prior notification than foreign systems. Prior notification submitted under the Japanese system is an important source of information not only in the prior screening process, but also in monitoring after the implementation of investment transactions, from the perspective of accurately dealing with national security, etc. Based on the awareness of this issue, the authorities are making further efforts to strengthen monitoring in order to identify cases of non-compliance in a timely and appropriate way and issue necessary orders or corrective measures in a flexible manner.

Summary of inward FDI screening systems in each country

provisional

		US	UK	France	Germany	Italy	Canada	Japan
Mandatory pre-	Thresholds	No numerical thresholds (Limited to transactions involving the acquisition of control or sensitive information)	25%	10%	10% / 20%	3% / 10%	33% (for companies above a certain size)	1%
pre-screening	Sectors subject to review	Designated sectors (Limited to critical technology, infrastructure and data-related)	Designated sectors	Designated sectors	Designated sectors	Designated sectors	All	Designated sectors
	orrective cervention	Review, divestiture orders etc. are possible even if they are not subject to mandatory pre- screening	Review, divestiture orders etc. are possible even if they are not subject to mandatory pre- screening	Divestiture orders etc. are possible for cases subject to mandatory pre- screening	Review, divestiture orders etc. are possible when acquiring more than 25% of shares even if they are not subject to mandatory pre- screening	Divestiture orders etc. are possible for cases subject to mandatory pre- screening	Review, divestiture orders etc. are possible even if they are not subject to mandatory pre- screening	Even if they are not subject to mandatory prescreening, if investors who use prior notification exemption fail to comply with exemption conditions, divestiture orders etc. are possible
m	umber of andatory -screenings	440	671	131	257	608	5	2,871

⁽note 1) Prepared based on the published data of each country. Thresholds and other information in the mandatory pre-screening row are for listed companies. The number of mandatory pre-screenings is based on the most recent published data at the time of writing for each country. (Japan, Apr 2023-Mar 2024; US, France and Italy, Jan-Dec 2022; UK, Apr 2022-Mar 2023; Germany, Jan-Dec 2023.)

⁽note 2)

For US, the 440 cases include the number of voluntary filings.

For Canada, the number of applications subject to net benefit review is five. In addition, there were 1,005 notifications which can be provided up to 30 days after the investment has been made.

For Japan, there is a prior notification exemption system (blanket exemption for foreign financial institutions (regardless of acquisition ratio); general exemption for general investors (acquisition ratio: 1%-10%)).

<Column 5> Factors to be Considered in Screening

The FEFTA foreign investment screening system reviews whether an inward direct investment transaction, as stipulated in Article 27 of FEFTA, satisfies any of the four requirements stipulated in Article 27, Paragraph 3, Item 1 of FEFTA ((1) impairing national security, (2) disturbing the maintenance of public order, (3) hindering the protection of public order, and (4) affecting the smooth functioning of the Japanese economy significantly and adversely. It also screens whether a specified acquisition, as stipulated in Article 28 of FEFTA, falls under the category of specified acquisitions that are highly likely to cause a situation that would compromise national security. It is important to disclose what the screening authorities will focus on in the screening in order to improve the transparency of the procedure and predictability for investors. National Diet deliberations on the FEFTA revision in 2019 and the supplementary resolution of the revised FEFTA called for the transparent and appropriate operation of the foreign investment screening system.

Given the above, the Ministry of Finance and other ministries responsible for relevant business sectors have published "Factors to be considered in authorities' screening" as follows:

- A) Factors regarding business operations of an investment target company: "the degree of impact of the investment on maintaining the production base and technologies in the business sectors that relate to the protection of national security, maintenance of public order, or safeguard of public safety;" "the possibility of leakage of technologies or information that relate to the protection of national security, maintenance of public order, and safeguarding of public safety, or use of these technologies or information against the objectives of protection of national security, maintenance of public order, or safeguard of public safety;" "the degree of impact of the investment on (1) terms and conditions of supply, (2) stable supply, or (3) quality of goods or services that relate to protection of national security, maintenance of public order, or safeguard of public safety, in ordinary and emergency situations".
- B) Factors regarding the attributes of a foreign investor: "attributes of the foreign investor, including its capital structure, beneficial ownership and business relationships, and the foreign investor's plan and track record of its behaviors relating to the investment;" "the degree of impact on the protection of national security, maintenance of public order, safeguard of public safety, or smooth functioning of the Japanese economy from international treaties and domestic laws and regulations with which the foreign investor needs to comply;" "track record of the foreign investor's compliance with FEFTA and equivalent or similar legislation of other jurisdictions.
- C) Factors regarding details of a foreign investor's investment and engagement in the investment target company: "the degree of impact of the investment on the investee company or the borrowing company in view of the number and percentage share of shares, equities, voting rights, subscription certificates or corporate bonds that have been acquired or are to be acquired by the foreign investor, or the amount and terms and conditions of the outstanding loan by the foreign investor;" "the possibility, and the degree of impact on the protection of national security and other domains, of the foreign investor's taking the following actions: (1) becoming, or having the investor's closely-related persons become, auditors or board members of the investee company, (2) proposing to the general shareholders meeting transfer or disposition of the investee company's business activities in the designated business sectors, and (3) obtaining, or proposing the disclosure of, secret non-public information about the investee company's technology and systems, or proposing changes in the investee company's internal rules, etc. on managing such information;"

During the screening, the authorities consider these factors while checking the contents of the notification and public, open-source information.

[Reference]

Ministry of Finance website: Factors to be considered in authorities' screening of prior notification for Inward Direct Investment and Specified Acquisition under the Foreign Exchange and Foreign Trade Act https://www.mof.go.jp/english/policy/international_policy/fdi/gaitamehou_20200508.htm (in English)

(3) Cooperation with Relevant Organizations in Japan and Overseas

Given the changes in the international economic and financial situation, such as a recent increase in inward direct investment and foreign investors' diversification of methods for exerting influence on Japanese companies, it is important for the Ministry of Finance and other ministries responsible for relevant business sectors to enhance their foreign investment screening capacity. This includes information gathering, in order to distinguish between inward direct investment transactions that are related to national security and sound ones that are not and to realize secure and prompt screening under the foreign investment screening system. For this reason, it is important for reviewing authorities to strengthen cooperation with relevant organizations in Japan and overseas and utilize these organizations' information for screening from the perspective of enforcing the system effectively. Therefore, the 2019 FEFTA revision included necessary measures, such as the establishment of provisions regarding requests for support from domestic relevant organizations (FEFTA Article 69-3) and those regarding information cooperation with foreign authorities (FEFTA Article 69-4). In recent years, the authorities have been making particular efforts to enhance cooperation with relevant organizations in Japan and overseas by holding regular meetings of relevant ministries for the purpose of sharing knowledge on inward direct investment trends and screening methods and by promoting the exchange of information with foreign authorities.

4. Status of System Implementation

(1) Prior notification

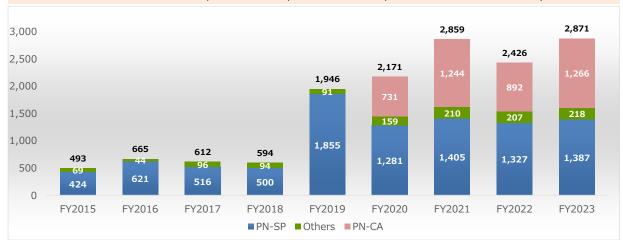
Prior notification is the basis for the enforcement of the foreign investment screening system and an important source of information that is used not only for screening but also for ex post facto monitoring and planning under the system. In particular, Japan's foreign investment screening system requires more prior notification than those in other countries (see 3 (2) above). For this reason, how to deal with foreign investors' failure to submit prior notification (a non-notified case) is one of the important policy issues related to the foreign investment screening system (see (7) below).

Recent prior notification statistics are as follows.

Number of Prior Notification(PN) from FY2015 to FY2023

- The 2019 amendment of the Foreign Exchange and Foreign Trade Act has lowered the threshold for prior notification for stock purchases (PN-SP) with regard to the acquisition of a listed company's stocks from 10% to 1%. The amendment also introduced mandatory prior notification for certain actions (PN-CA), namely, (i)voting at the shareholder's meeting for nomination of the foreign investor itself or a related person as a board member of the investee company and (ii)voting at the shareholder's meeting for a proposal, made by those foreign investors, to transfer or dispose of the investee company's business activities in the designated business sectors. On the other hand, the amendment introduced an exemption scheme for PN-SP for investors who comply with certain conditions.
- The number of prior-notifications for FY2023 is as follows.

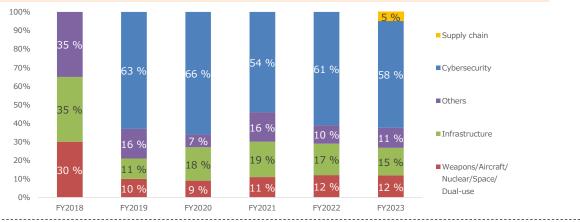
 (Note: The number for 2020 is not comparable with other years due to the full implementation of FEFTA in June 2020.)



(Note) **Others** include prior notifications for change of business purposes, making loans, bond acquisition, transfers of shares, establishment of a branch office, acquisitions of business and joint exercise of voting rights, etc.

Prior Notifications by Business Sector

 In FY2023, sectors related to cybersecurity (e.g. data processing and information services, software services, integrated circuits, semiconductor memory media, etc.) which were added to the designated business sectors in August 2019, accounted for 58%.



Reference: Designated Business Sectors

- Cybersecurity (Data processing/software services, Storage/memory/processing device etc.)
- Weapons Aircraft
- Nuclear facilities
- Metal mining etc. of critical minerals
 Construction service business etc. which improves or maintains port facilities on Designated Remote
 *Nov 2021 added _
- Electricity

- Telecommunica >
- Water supply Railways
- Petroleum Heat supply
- Broadcasting Public transportation
- Security services Biological chemicals > Agriculture, Forestry
- Leather manufacturing
- Air transportation
- Maritime transportation Pharmaceutical manufacturing Specially-controlled
 - medical devices manufacturing *July 2020 adde Supply chain *May 2023 added
- (Note 1) The prior notifications for companies which conduct business in multiple business sectors are counted in each of the sectors. Please refer to the next page for the numbers of each sector. (Note 2) The figures for FY2019 and prior show a breakdown of PN-SP, while FY2020 onwards shows a breakdown for all prior notifications. (Note 3) Telecommunications businesses are included in the Cybersecurity from FY2019 onwards.

(Reference) The number of Business Sectors in Prior Notifications

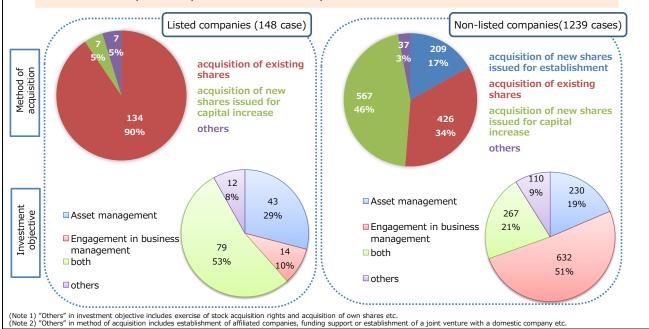
	FY2017	FY2018	FY2019		FY2	020			FY20	021			FY20)22			FY2	023	
	F12017	F12016	F12019	PN-SP	Others	PN-CA	Total												
Weapons, etc.	171	233	188	100	6	59	165	196	10	134	340	121	9	103	233	175	14	109	29
Aircraft	2	19	23	18	0	4	22	11	2	10	23	17	2	18	37	19	0	7	2
Nuclear facilities	2	12	10	2	0	2	4	2	1	3	6	10	0	7	17	7	1	8	1
Space	3	15	16	12	0	4	16	25	1	9	35	17	0	10	27	22	3	28	5
Cybersecurity	-	-	1,457	953	56	590	1,599	994	105	863	1,962	984	104	696	1,784	952	103	978	2,03
Metal mining etc. of critical minerals	-	-	-	-	-	-	-	4	0	0	4	4	0	0	4	7	0	0	
Construction service business etc. which improves or maintains port facilities on Designated Remote Islands	-	-	-			-		4	0	0	4	8	6	0	14	5	3	0	8
Secure Stable Supply Chains		-		-		-		-			-		-	-		82	10	69	16
Electricity/Gas, etc.	395	318	235	255	87	44	386	328	96	83	507	225	72	77	374	254	85	58	39
Telecommunications	18	14	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Broadcasting	2	7	2	9	0	2	11	14	0	16	30	3	1	0	4	9	0	15	24
Water supply	5	3	6	1	0	2	3	2	0	0	2	3	0	2	5	2	0	0	
Railways	1	3	2	1	0	0	1	3	1	4	8	26	9	1	36	18	3	0	2
Public transportation	9	0	0	0	0	0	0	0	0	0	0	2	0	0	2	5	0	1	
Biological chemicals/Pharmaceutical manufacturing, etc.	14	19	34	27	4	45	76	69	3	72	144	24	5	80	109	39	12	96	14
Security services	44	40	77	12	0	9	21	57	1	27	85	27	1	18	46	35	1	27	6
Agriculture, Forestry and Fisheries	76	94	96	37	5	11	53	69	0	62	131	47	5	44	96	59	2	57	118
Petroleum	53	49	46	15	1	22	38	75	2	54	131	28	3	47	78	46	3	33	8:
Leather manufacturing	31	10	29	2	0	0	2	0	0	4	4	5	0	5	10	10	1	0	1
Air transportation	33	31	11	4	1	2	7	2	1	4	7	3	3	0	6	3	0	4	
Maritime transportation	33	36	31	5	0	6	11	49	1	162	212	3	0	23	26	8	0	32	4
Total number of PN	612	594	1,946	1,281	159	731	2,171	1,405	210	1,244	2,859	1,327	207	892	2,426	1,387	218	1,266	2,87
Sum of sectors in PN	892	903	2,263	1,453	160	802	2,415	1,904	224	1,507	3,635	1,557	220	1,131	2,908	1,757	241	1,522	3,520

(Note 1) The prior notifications for companies which conduct business in multiple business sectors are counted in each of the sectors. (Note 2) "PN-SP" is Prior Notification for Stock Purchases. "Others" is change of business purpose, making of loan, bond-acquisition, transfers of shares, establishment of branch office, acquisition of business and joint exercise of voting rights, etc. "PN-CA" is Prior Notification for Certain

(Note 3) Telecommunications businesses are counted as Cybersecurity from FY2019 onwards.

PN-SP by Acquisition Method and Investment Objective (FY2023)

- The number of PN-SP for listed companies is 148, far smaller than that for non-listed companies, 1,239.
- Regarding methods of acquisition, approximately 90% of the acquisitions of listed companies were made through acquisitions of existing shares, including from the stock market. In contrast, non-listed companies' shares are largely acquired by foreign investors through capital increases.
- Regarding investment objectives, there is a higher percentage of "Engagement in business management" for non-listed companies compared to that of listed companies.



Number of Prior-Notification for Stock Purchases (PN-SP) by countries (FY2023)

- Excluding Japanese investors, the largest number of PN-SP is submitted by US investors, followed by those in the Cayman Islands and Singapore.
- The large number of PN-SP from Japanese investors is due to the provision of the Foreign Exchange and Foreign Trade Act that treats Japanese companies as foreign investors where 50% or more of their voting rights are directly or indirectly held by non-resident individuals or foreign entities.

PN-SP by the investor's home country

	Listed company	Non-listed company	total
Japan	44	406	450
US	22	250	272
Cayman Islands	3	145	148
Singapore	38	102	140
Hong Kong	5	52	57
South Korea	0	36	36
UK	0	30	30
Taiwan	0	28	28
Netherlands	0	23	23
China	0	22	22
Canada	13	7	20
British Virgin Islands	3	16	19
France	2	17	19
Germany	0	18	18
Vietnam	0	13	13
Switzerland	0	11	11
British Bermuda Islands	0	9	9
Saudi Arabia	8	0	8
Australia	1	7	8 7
India	0	7	7
Israel	0	4	4
Luxembourg	0	3	3
Ireland	1	2	3 3 2 1
Sweden	0	2	2
Thailand	0	1	1
Others	8	28	36
total	148	1239	1387

PN-SP by the ultimate parent company of the investor whose home country is Japan

Listed Non-listed US 100 106 Japan 16 86 Singapore 75 23 75 25 Cayman Islands 0 France Luxembourg Denmark Germany China 0 Hong Kong South Korea Netherlands Australia Spain Others 37 40 Not applicable 9 46 55 450 PN-SP by the ultimate parent company of the investor whose home country is the Cayman Islands

Listed	Non-listed	total
company	company	total
1	65	66
0	45	45
0	17	17
0	11	11
0	4	4
0	1	1
0	1	1
2	1	3
0	0	0
3	145	148
	company 1 0 0 0 0 0 0 0 2 0	company company 1 65 0 45 0 17 0 11 0 4 0 1 0 1 2 1 0 0 0 0

(Note 1) The case where the home country of the investor is "Japan" and the ultimate parent company is also "Japan" is when a subsidiary is a filer and has a parent company in Japan, and multiple foreign corporations hold more than 50% of the voting rights of the parent company in total, but no single foreign corporation holds more than 50%.

(Note 2) The case where the home country of the investor is "Japan" and the ultimate parent company is "N/A", is when multiple foreign corporations hold more than 50% of voting rights of the investor in total, but no single foreign corporation holds more than 50% of the voting rights.

(Note 3) If the investor is a non-resident individual, classification is based on the nationality of the individual.

(2) Average screening period

Under the FEFTA foreign investment screening system, foreign investors who have submitted the notification are prohibited from implementing the notified investment transactions within 30 calendar days from the notification receipt in order for the Minister of Finance and ministers responsible for relevant business sectors to screen whether investment transactions subject to prior notification impair national security, etc. (the investment prohibition period can be extended up to four months). However, the investment prohibition period may be shortened if an investment transaction does not fall under the category of those that may cause any situation that impairs national security, etc. The authorities screen prior notification on a risk basis and complete screening promptly and flexibly if the investment transactions in question do not fall under the category of those that may cause any situation that impairs national security, etc. In FY2023, screening was completed within two weeks for about 70% of prior notifications. The average screening period was 9.1 days.

(3) Withdrawal of prior notification

In cases where prior notification is required, foreign investors may submit prior notification up to six months before planned investment transaction dates. In practice, however, they may communicate with the authorities (the Ministry of Finance and other ministries responsible for relevant business sectors) before or after official prior notification for individual inquiries regarding the system, including how to fill the notification form and whether prior notification is required. Regarding investment transactions that have a risk of impairing national security, etc., the authorities may check facts about the details of their transactions in order to ascertain the actual situation for appropriate screening. During such communications with the authorities, foreign investors may withdraw their prior notification and cancel their planned investment transactions or revise their notification for resubmission.

The numbers of prior notification withdrawals in recent years are as follows:

FY2020	FY2021	FY2022	FY2023
242	239	274	399
(2,171)	(2,859)	(2,426)	(2,871)

^{*} In brackets are the total numbers of prior notifications.

(4) Requiring report

Foreign investors are required to submit post-investment reports on their inward direct investment transactions under FEFTA Article 55-5. In addition, the Minister of Finance and ministers responsible for relevant business sectors may order foreign investors to report on matters related to their inward direct investment transactions "to the extent necessary for achieving the purpose of this Act" (requiring report) (FEFTA Article 55-8).

In the operation of the foreign investment screening system, the Minister of Finance and ministers responsible for relevant business sectors endeavor to obtain the necessary facts through communications with foreign investors and their target companies from the perspective of proper FEFTA enforcement, including the screening of prior notification. If it is necessary to accurately confirm important facts that will lead to a judgment on the necessity of further legal action under FEFTA or if it is difficult to promptly confirm the facts only through voluntary communications, for example, a statutory requirement of reporting may be issued from the perspective of ensuring the effective enforcement of the system. Failure to comply with statutory requirement of reporting or false reporting to statutory requirement of reporting may be subject to penalty.

The numbers of report requests in recent years are as follows:

FY2020	FY2021	FY2022	FY2023
2	1	2	1

(5) Order for modification, discontinuance/ Order for measures

The Minister of Finance and ministers responsible for relevant business sectors may order foreign investors to take necessary measures, such as the disposal of all or part of shares or equity acquired through their inward direct investment transactions, if having taken prescribed procedures, such as hearing opinions from the Council on Foreign Transactions after recognizing that such investors' inward direct investment transactions or their specified acquisitions are related to national security, etc. in cases (1) to (3) and (6) below, or if in case (4) or (5) below (FEFTA Article 29).

- (1) If the transactions are implemented without prior notification
- (2) If the transactions are implemented before the end of the investment prohibition period before the clearance of screening
- (3) If false prior notification is submitted
- (4) If the foreign investors fail to comply with the recommendations they accepted for changes in the inward direct investment transactions in question, or violate orders for such changes
- (5) If the foreign investors fail to comply with the recommendations they accepted for the cancellation of the inward direct investment transactions in question, or violate orders for the cancellation
- (6) If foreign investors who use the prior notification exemption system for inward direct investment transactions violate orders for recommended measures to comply with the exemption conditions

Since the 2017 FEFTA revision when provisions for specified acquisition and orders for measures were introduced, there have been no recommendation or order for measures based on FEFTA Article 29 and there have been no recommendations or orders to modify or discontinue the investment based on Article 27 and Article 28.

The authorities have various methods for dealing with national security and other risks, including not only orders for measures such as divestiture orders, but also statutory requirement of reporting (see 4. (4)), and responses through administrative guidance regarding prior notification screening and ex post facto monitoring. These methods are used appropriately in accordance with a specific situation.

(6) Penalties

From the viewpoint of ensuring the enforcement of the foreign investment screening system, FEFTA has various penalty provisions. Specifically, FEFTA Article 70 stipulates that violations such as those of the prior notification obligation and orders for transaction changes by the Minister of Finance and ministers responsible for relevant business sectors shall be subject to imprisonment for not more than three years, a fine of not more than 1 million yen, or both. If three times the value of the subject matter of a violation exceeds 1 million yen, the fine is not more than three times that value. In addition, FEFTA Article 71 imposes a penalty of imprisonment for up to six months or a fine of up to 500,000 yen for violations regarding reporting obligations and on-site inspections.

No penalty has been imposed since the 2019 FEFTA revision that established the present basic framework for the inward direct investment screening system.

(7) Non-notified cases

Under the FEFTA inward direct investment screening system, if a foreign investor who is required to submit prior notification regarding an inward direct investment transaction fails to do so (hereinafter referred to as "Non-notified cases"), the investor may become subject to an order for measures as stipulated in FEFTA Article 29, being ordered by the authorities (the Ministry of Finance and other ministries responsible for relevant business sectors) to take necessary measures, such as divestiture orders.

In deciding on the necessary measures, the authorities may consider the circumstances of the failure, such as whether the violation was intentional, the circumstances under which the violation was found (whether it was voluntarily reported by the investor in question or found by the authorities), whether the investor reported the violation to the authorities immediately after becoming aware of the violation, whether the investor took measures to conceal the violation, and whether the investor repeated or continued the violation. If the violation is recognized as highly malicious, tough measures may be taken. In the event that a non-notified case is found, the authorities first request

the foreign investor in question to prepare and submit a case investigation form regarding the outline of the violation, the circumstances under which the violation was found, the management system and the reason for the violation, and measures to prevent the recurrence of the violation, and then take specific measures based on the responses.

The detection of non-notified cases is extremely important from the viewpoint of accurately preventing the leakage of technological information related to national security, etc., and from the perspective of ensuring the appropriate enforcement of the inward direct investment screening system. It is an area that the authorities have been focusing on in recent years. As a result, the number of non-notified cases detected by the authorities has been increasing, as shown below. There have been cases where violations in multiple years were found when the latest violations were detected. In reality, there is a considerable number of minor notification failure cases that arise from a lack of awareness of the system and are less malicious. Thus, the authorities are making efforts to inform related industry groups about the system, including professionals who often act as agents in FEFTA procedures. It is our policy to make further efforts to detect non-notified cases through measures such as the dissemination of the system and conducting analysis using public announcements and information regarding companies in designated business sectors and foreign investors.

The numbers of non-notified cases (based on the number of case investigation forms) in recent years are as follows:

FY2021	FY2022	FY2023
133	224	238

(8) Prior notification exemption system

Foreign investors who meet certain requirements can use the prior notification exemption system only if they comply with certain conditions, such as pledging to refrain from being appointed as director and from accessing secret non-public technological information at target companies (see 2. (2)).

Under these circumstances, it is important for the authorities to enforce the system effectively, including taking strict measures in accordance with laws and regulations as necessary, so that the use of the prior notification exemption system by foreign investors who are not qualified to use the system and violations of the exemption conditions after the use of the system do not risk harming national security, etc. Accordingly, the authorities continuously monitor foreign investors who use the prior notification exemption system, including checking the status of their compliance with the exemption conditions, based on their attributes and the details of their transactions.

The numbers of post-investment reports under the prior notification exemption system are as follows:

FY2020	FY2021	FY2022	FY2023
960	842	756	640
(623)	(604)	(546)	(426)

^{*} The above are the numbers of post-investment reports submitted by foreign investors after an investment has been made using the prior notifications exemption system.

In brackets are the numbers of blanket exemptions for foreign financial institutions.