Appraisal Rights in Japanese Corporate Law

Moritz Bälz

I. Introduction

The purpose of this paper is to analyze the role of appraisal rights in protecting minority shareholders of Japanese corporations. Unlike Japanese derivative suits, appraisals in Japanese corporate law have never really enjoyed much attention by Western scholars. This is rather surprising given that the development of the Japanese Commercial Code (CC) seems to tell a great success story of the appraisal remedy. Especially since the 1990s, various amendments to the Commercial Code have constantly broadened the

scope of appraisal rights. Whenever policymakers introduced a new transaction form, such as share exchanges, share transfers or corporate splits, they added appraisal rights in order to strike the right balance. Furthermore, the mere existence of appraisal rights in Japan is one reason why a recent, much-quoted survey on investor protection around the world has credited Japanese law with comparatively strong investor protection.\(^4\) This result contrasts sharply with Japan’s allegedly poor record in promoting shareholder interest\(^5\) and might further underline the necessity of a close examination of the effectiveness of the appraisal remedy in Japanese Law.

In assessing Japanese appraisal rights, I propose to focus on the substantive and procedural rules on appraisal.\(^6\) This is primarily because empirical evidence on the use of appraisal rights in Japan is difficult to gather.\(^7\) The few court decisions on appraisal rights, which have been published, do not provide a clear picture. Nor does the limited number of published decisions by itself allow conclusions about the practical importance of appraisal rights for minority shareholders. Theoretically, the existence of only a few court decisions could be a hint for the limited practical usefulness of the remedy as well as an indication for a high ratio of successful out-of-court settlements.

The structure of the paper is the following. First, I will describe the origins and aims of appraisal rights in Japan (II.) and how the Japanese legislator has gradually extended their scope of application (III.). Second, I will outline the procedure of appraisal (IV.), how Japanese courts assess fair value (V.), and the relationship of appraisal rights to other remedies (VI.). Finally, to complete my evaluation of the Japanese appraisal right provisions, I will glance on some differences between the Japanese model and appraisal rights in the United States (VII).

\(^4\) R. La Porta / F. Lopez-de-Silanes / A. Shleifer / R.W. Vishny, Law and Finance: 106 Journal of Political Economy 1113, 1128-1131 (1998). The survey indexes the laws of the world according to the degree to which they protect the interests of minority shareholders. Japanese law scores comparatively high. Japan receives four out of six possible credits on the so-called anti-director index, compared to five for the US and one for Germany. This is partly because Japanese law provides for an “oppressed minority mechanism”, a term by which the authors refer to remedies such as derivative suits and appraisal rights. See also R. La Porta / F. Lopez-de-Silanes / A. Shleifer / R.W. Vishny, Investor Protection: Origins, Consequences, Reform 1, 18 (1999) (manuscript available for download at <http://post.economics.harvard.edu/hier/1999papers/HIER1883.pdf> describing Japan’s minority shareholder protection as “fairly good”.


\(^6\) I will concentrate on the rules for corporations organized in the form of stock corporations (kabushiki kaisha, K.K.), which are part of the Commercial Code. Articles without further specification refer to the Commercial Code (CC). Limited liability corporations (yûgen kaisha), which are regulated in the Law on Limited Liability Companies (Yûgen kaisha-hô, Law No. 75/1938, LLCL), will only be covered occasionally. The dominant corporate form in Japan today is the stock corporation. See I. Kawamoto / M. Kishida / A. Morita / Y. Kawaguchi, Nihon no kaisha-hô [The Corporate Law of Japan] (4th ed. 2001) no.16.

\(^7\) Statistics do not exist. Hayakawa, supra note 2, at 623 footnote 49.
The result of my analysis casts serious doubt on the effectiveness of the Japanese appraisal right provisions in their present state. Even if the substantive rules on appraisal in the Japanese Commercial Code could in principle guarantee adequate minority shareholder protection, high procedural barriers seem to impede the achievement of this objective. Should future empirical and more comprehensive comparative research confirm these findings, a revision of the procedural rules on appraisal might be desirable. The promise is that appraisal rights thus could really become a viable weapon in the hands of minority shareholders and allow Japan to reap the benefits of strong shareholder protection, among them improved corporate governance.8

II. ORIGINS AND AIMS OF APPRAISAL RIGHTS IN JAPANESE LAW

Appraisal rights are an American invention. Traditionally, the Common Law required unanimity for fundamental changes of the corporate structure. When the size of corporations grew and ownership became more dispersed, obtaining such unanimous decisions on fundamental changes was no longer feasible. In order to create more flexibility and at the same time strike the right social balance, majority decisions on certain fundamental transactions were introduced and simultaneously dissenting shareholders for the first time were given the right to sell their shares back to the company at fair value.9

In Japan, whose company law derives from continental, especially German sources, appraisal rights (kaitori seikyû-ken) were first introduced in 1950 to balance broader competences of the board.10 At the time the majority of Japanese legal commentators opposed the reform. Appraisal rights were considered inconsistent with the majority principle. As appraisal effectively allows for paying back paid-in capital, many regarded it as a violation of the principle of capital maintenance (shihon iji gensoku) that stands at the very center of the legal capital system. Furthermore, critics expected difficulties with respect to the process of determining the value of the minority share as well as potential hazards of abuse. Only gradually appraisal rights gained support as an instrument of minority shareholder protection.11

The Commercial Code does not distinguish between appraisal rights in the case of public or private companies, nor does it exclude shareholders of listed companies from the scope of appraisal rights (“market-out” exception) as it is known from American law.12

8 See LA PORTA ET AL., Investor Protection, supra note 4, at 16 et seq.
10 KAWAMOTO ET AL., supra note 6, at no. 73; HAYAKAWA, supra note 2, at 613.
12 See, e.g., Delaware General Corporation Act (DGCL) § 262(a)(1) and Revised Model Business Corporation Act (RMBCA) § 13.02(b)(1).
Nevertheless, Japanese scholars acknowledge that in the case of corporations, which are listed at the stock exchange, dissenting shareholders normally can sell their shares into a liquid market at any time, while minority shareholders in closely held corporations lack such an uncomplicated exit option.¹³

III. Scope of Application

Today the Japanese Commercial Code provides for appraisal rights in almost all cases of fundamental change to the corporate structure. An exception exists in the event of an amendment of the object of the corporation (Art. 166).¹⁴ As a general principle appraisal rights were originally tied to the requirement of a special shareholder resolution (toku-betsu ketsugi), i.e. a supermajority of two thirds of the votes present with a quorum of 50% of the total shares outstanding (Art. 343). I will describe some modifications of this principle and the gradual extension of the scope of appraisal rights in the following:¹⁵

1. Merger, Transfer of Business, and Restriction of Transferability of Shares

When appraisal rights were first introduced in 1950¹⁶, their scope was limited to mergers (gappei, Artt. 56, 408-3) and transfers of all or an important part of the company business (eigyô jôto, Artt. 245 para. 1 no. 1, 245-2).¹⁷ Both transactions require a special shareholder vote. In the case of a merger the shareholders of all constituent companies, i.e. any company disappearing due to the merger as well as the surviving company, are entitled to appraisal rights. In the case of a transfer of all or an important part of the business of the company the shareholders have appraisal rights unless simultaneously with the resolution on the transfer of business a resolution for dissolution is adopted (Art. 245-2 proviso). The rationale given for this exception is that shareholders in this event receive the dissolution value of their shares by means of the dissolution procedure, while creditors might be harmed if the company purchased shares from dissenting shareholders during the winding up process.¹⁸

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¹³ See SHISHIDO, supra note 11, at § 245-2 no. 2.
¹⁴ This inconsistency has frequently been criticized: SEKIGUCHI, supra note 11, at 436; HAYAKAWA, supra note 2, at 614.
¹⁵ For an overview of the provisions granting appraisal rights see the table infra.
¹⁶ For the historical development of appraisal rights in Japan see SEKIGUCHI, supra note 11, at 430; HAYAKAWA, supra note 2, at 613 et seq.
¹⁷ The appraisal right of Art. 245-2 also applies in the case of the making, alteration or rescission of a contract for leasing the whole business, for giving a mandate to manage the business, for sharing with another person the entire profits and losses from the business, or similar contracts (Art. 245 para. 1 no. 2) as well as in the case of a takeover of the whole business of another company (eigyô yuzuriuke no. 3).
¹⁸ See SHISHIDO, supra note 11, at § 245-2 no. 4. From a policy point of view this proviso is not beyond doubt, as shareholders are not necessarily compensated for an unfavorable transfer of business in liquidation. Id.
In 1966 appraisal rights were introduced in the event of an alteration of the corporate charter restricting the transferability of shares by requiring board approval (today Artt. 348 para. 1, 349). Such alteration requires only a simple majority of the votes. However, there is a quorum of 2/3 of the total shares outstanding. The shareholders who have acquired stock on the assumption they would be free to sell it at any time to any person, are thus given the right to sell their stock to the company when this freedom becomes restricted by such alteration.\textsuperscript{19}

2. Transformation, Share Exchange, and Corporate Split

The scope of the appraisal remedy has considerably been broadened in the 1990s, when the Japanese legislator made various efforts to boost the economy by making Japanese corporate law more flexible. In 1990 the legislator introduced rules, which allow for a transformation (soshiki saihen) of stock companies into limited liability companies (Art. 64-2 LLCL) and vice versa (Artt. 67 para. 6, 64-2 LLCL).\textsuperscript{20} In both cases shareholders are provided with appraisal rights.

In 1997, the Japanese legislator lifted the ban on holding companies. Subsequently, in 1999 the Commercial Code was amended to introduce new mechanisms to allow for a facilitated creation of holding companies. Rules for shares exchanges (kabushiki kôkan) now enable a parent company to transform a subsidiary into a wholly-owned subsidiary by forcing the minority shareholders of the subsidiary to accept shares in the parent company in exchange for their shares in the subsidiary (Artt. 352, 353).\textsuperscript{21} The transaction requires a special shareholder resolution. In order to protect shareholders of the parent and the subsidiary against an unfair exchange ratio in such transactions, they are both granted appraisal rights. The legislator viewed the quality of the transaction as an organizational act and considered it not enough to give shareholders the right to seek an injunction against the issuance of the new shares or have the issuance voided by the court.\textsuperscript{22} A related transaction device introduced at the same time, the so-called share

\textsuperscript{19} Furthermore, since 1981 a shareholder holding fractional shares (hakabu) of a total of less than one share has the right to sell these fractional shares to the company (Art. 220-6 today). A similar right was enjoyed by unit share shareholders holding unit shares of less than one unit during the existence of the unit share system (tan’i kabu seido) from 1981 to 2001 (Art. 19 para. 1 of the Supplementary Provisions of the Law No. 74, 1981 amending the Commercial Code). These rights, though sometimes also referred to as appraisal rights, shall not be considered in this paper, as their aim significantly differs from appraisal rights in the case of fundamental changes to the corporate structure.

\textsuperscript{20} The step requires the same kind of resolution as the restriction of transferability of shares (Art. 348). See supra, at 1.


\textsuperscript{22} H. Maeda, Kaisha-hô nyûmon [Introduction to Corporate Law] no. 727-16 (7th ed. 2000). Prof. Maeda is the head of the legislative commission (hôsei shingi-kai), which drafted the amendments of the Commercial Code in recent years.
transfer (kabushiki iten), allows a company to transform itself into a wholly-owned subsidiary of another newly founded company (Art. 364). Again appraisal rights are supposed to strike the right balance.

In 2000, new rules on corporate splits (kaisha bunkatsu) were adopted. This form of transaction enables a company (the splitting company) to transfer its entire business or a part of it to another company (the receiving company), which either is simultaneously founded (split for new foundation, shinsetsu bunkatsu, Artt. 373, 374), or which already exists (split for absorption, kyūshū bunkatsu, Artt. 374-16, 374-17). The receiving company in exchange issues shares either only to the splitting company itself (butteki bunkatsu), or as well or exclusively to the shareholders of the splitting company (jinteki bunkatsu). Again, the transaction requires a special shareholder vote and dissenting shareholders of the companies involved have appraisal rights.

3. Small-Scale Transactions
   
a) Introduction of Facilitated Procedures for Small-Scale Transactions

To provide Japanese companies with more flexibility, today certain small-scale transactions do no longer require shareholder approval. In 1997, such facilitated procedures were introduced for mergers. On the side of the surviving company shareholder approval is no longer required, provided that the shares issued on occasion of the merger do not exceed 20% of the total number of shares outstanding of the surviving company and no cash amount is paid to the shareholders of the merged company in excess of 1/50 of the amount of the surviving company’s net assets (kan’i gappei, Art. 413-3 para. 1). The rationale is that as long as the shares of the surviving company are not diluted beyond a certain scale, a time-consuming and costly shareholder vote would be inefficient and a board resolution should suffice.

Today similar provisions exist in the Commercial Code for small-scale takeovers of businesses (kan’i eigyō yuzuriuke, Art. 245-5 para. 1), small-scale share exchanges (kan’i kabushiki kōkan, Art. 358), and small-scale corporate splits (kan’i bunkatsu, Artt. 374-6, 374-22, 374-23).23

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23 In the case of corporate splits for absorption the procedure can be facilitated on the side of the receiving company (Art. 374-23) or on the side of the splitting company (if the book value of the business, which is split off, does not amount to more than 5% of the total book value of the company’s assets, Art. 374-22), or even both at a time. MAEDA, supra note 22, at no. 728-23. The latter applies, if the transferred part of the business is comparatively small as to both, the splitting company’s total assets (less than 1/20) and the receiving company’s assets (not requiring issuance of more than 20% of new stock or payment of cash in excess of 1/50 of the net assets).
b) **Appraisal Rights in the Case of Small-Scale Transactions**

Japanese law provides those shareholders who are not entitled to vote on such facilitated transactions with appraisal rights. The Japanese legislator feared that otherwise minority shareholders would have no effective remedy to fight, e.g., an unfair exchange ratio of a merger.\(^{24}\) In this context it should be noted that fiduciary duty standards in the case of mergers are rather scarcely developed and ambiguous in Japan.\(^{25}\)

In the event of facilitated corporate splits appraisal rights are only granted if the splitting company transfers the part of its business to an existing company (split for absorption) and if the split is facilitated on the side of the receiving company (Art. 374-23). An example would be that an existing company A receives part of the business of another company B and in exchange issues new shares either to company A or to company A’s shareholders, but no more than 20% of its total number of shares outstanding. In addition the total amount of cash paid to company A or its shareholders may not exceed 1/50 of company B’s net assets. Under these conditions approval of company B shareholders is not required. Nevertheless, the latter are entitled to appraisal rights (Art. 374-23 para. 5). In two more constellations in which the Commercial Code allows for facilitated split procedures, appraisal rights are excluded:

1. If the business of the splitting company is transferred to a company newly established on that occasion (split for new foundation), the shareholders of the splitting company do not enjoy appraisal rights (Art. 374-6 para. 3). The reason given is that the facilitated procedure for splits for new foundation is only available if all newly issued shares are issued to the splitting company \(\text{(butteki bunkatsu)}\)\(^{26}\) and the transferred business is comparatively small. Appraisal rights thus are considered unnecessary.\(^{27}\) In addition, granting appraisal rights even in the case of the transfer of a comparatively minor part of the business to the newly established subsidiary would contradict the rules on business transfers, which require a shareholder vote and give rise to appraisal rights only if \textit{all or an important part} of the business \(\text{(eigyô no zenbu mata wa jûyô naru ichibu)}\) is to be transferred (Artt. 245 para. 1, 245-2).\(^{28}\)

2. For the same reasons\(^{29}\) appraisal rights are excluded if a split for absorption is performed through a facilitated procedure on the side of the splitting company (Art. 374-22 para. 3).

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\(^{26}\) The shareholders of the splitting company shall not become shareholders of the newly established subsidiary without having a say. Therefore it is not possible to make use of the facilitated procedure and issuing shares to the splitting company’s shareholders at the same time \(\text{(jinteki bunkatsu)}\). For the same reason there is no such thing as a facilitated share transfer. MAEDA, *supra* note 22, at no. 728-23.

\(^{27}\) MAEDA, *supra* note 22, at no. 728-24.

\(^{28}\) MAEDA, *supra* note 22, at no. 728-24.

\(^{29}\) MAEDA, *supra* note 22, at no. 728-39.
### 4. Overview: Forms of Transactions and Appraisal Rights

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Appraisal Rights</th>
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<td><strong>Business transfer, lease of business, takeover of business, etc.</strong></td>
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<tr>
<td>regular: Art. 245 para. 1 CC</td>
<td>Art. 245-2 CC (unless simultaneously resolution for dissolution, Art. 245-2 proviso CC)</td>
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<td><strong>Share exchange</strong></td>
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<td>Art. 364 CC</td>
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<tr>
<td>(no small-scale procedure)</td>
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<tr>
<td><strong>Split for new foundation</strong> (rules for limited liability companies in brackets)</td>
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<tr>
<td><strong>butteki</strong> (=all shares issued to splitting company)</td>
<td></td>
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<tr>
<td>regular: Artt. 373, 374 CC (Artt. 63-2, 63-3 LLCL)</td>
<td>Art. 374-3 CC (Artt. 63-6 LLCL, 374-3 CC)</td>
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<td>small scale: Art. 374-6 CC</td>
<td><strong>appraisal excluded</strong> (Art. 374-6 para. 3 CC)</td>
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<tr>
<td><strong>jinteki</strong> (= some or all shares issued to shareholders of splitting company)</td>
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</tr>
<tr>
<td>regular: Art. 374 CC (Artt. 63-2, 63-3 LLCL)</td>
<td>Art. 374-3 CC (Artt. 63-6 LLCL, 374-3 CC)</td>
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<tr>
<td>(no small-scale procedure)</td>
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<tr>
<td><strong>Split for absorption</strong> (rules for limited liability companies in brackets)</td>
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<tr>
<td><strong>butteki</strong> (=all shares issued to splitting company)</td>
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<tr>
<td>regular: Artt. 374-16, 374-17 CC (Art. 63-7 LLCL)</td>
<td>Artt. 374-31 para. 3, 374-3 CC (Artt. 63-9 para. 3, 374-3 CC)</td>
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<tr>
<td>small-scale on side of splitting company: Art. 374-22 CC</td>
<td><strong>appraisal excluded</strong> (Art. 374-22 para. 3 CC)</td>
</tr>
<tr>
<td>small-scale on side of receiving company: Art. 374-23 CC</td>
<td>Art. 374-23 para. 5 to 7 CC</td>
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<tr>
<td><strong>jinteki</strong> (= some or all shares issued to shareholders of splitting company)</td>
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</tr>
<tr>
<td>regular: Artt. 374-16, 374-17 CC (Art. 63-7 LLCL)</td>
<td>Artt. 374-31, 374-3 CC (Artt. 63-9, 374-3 CC)</td>
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<tr>
<td>(no small-scale procedure on side of splitting company)</td>
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<td>small-scale on side of receiving company: Art. 374-23 CC</td>
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<td><strong>Transformation of K.K. into LLC</strong></td>
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<td>Art. 67 LLCL</td>
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IV. PROCEDURE

In order to exercise the appraisal remedy a dissenting shareholder has to go through three steps. The procedure is in principle the same in all constellations allowing for appraisal rights:

1. Written Objection Prior to the Shareholder Meeting

First, the shareholder has to notify the company in writing prior to the shareholder meeting, which is to vote on the proposed transaction, that he intends to object to the proposal. A special form is not required, nor need the reasons for the objections or the number of shares held by the shareholder be stated. The notice has to actually reach the company before the beginning of the shareholder meeting. The company is under an obligation to include the essential information of the proposed transaction in the invitation for the shareholder meeting, which is to adopt the resolution. If the company fails to do so, and the shareholder thus has no opportunity to object, it is assumed that the shareholder is entitled to appraisal even without the written notice. The written notice is supposed to give the board the opportunity to rethink the proposal and to enable the other shareholders to adjust their voting behavior according to the number of objections the company has received. Whether this actually works in practice is doubtful, as dissenting shareholders may hand in their written objection to the company at the last minute before the shareholder meeting is opened, and there is no mechanism in place to let the other shareholders know how many written objections the company has received.

2. Voting Against the Proposal on the Shareholder Meeting

Secondly, the shareholder has to vote against the proposal on the shareholder meeting scheduled to vote on the transaction. He may do so by attending in person or by proxy.
voting (Art. 239 para. 3). Furthermore, Japanese law provides for shareholder voting by letter if the company has one thousand shareholders or more. However, companies are not compelled to offer this form of voting, as long as they accept proxy voting. In the case of voting by proxy a proxy card sent to the company stating “no” arguably fulfills the requirement of prior written objection. However, in addition the proxy must actually vote against the proposed transaction. If the shareholder has validly voted “no” by letter, this letter also fulfills the requirement of objecting to the proposal prior to the shareholder meeting.

Since it is required that the shareholder votes against the proposal, in principle only shareholders entitled to vote can have appraisal rights. Non-voting shares only grant appraisal rights in exceptional situations, when they are entitled to vote, e.g., because no dividends have been paid (Art. 242 para. 1).

The appraisal right is voided if the shareholder transfers his shares to a third person after an appraisal right has accrued. However, if the shareholder is succeeded by way of universal succession, e.g. due to a merger or due to inheritance, the appraisal right is transferred. Courts have recognized appraisal rights even in cases where an investor bought shares only after the proposed transaction had been announced.

36 If a proxy casts some votes in favor and some votes against the proposed transaction in order to reflect the various intentions of the beneficial owners, the shares voted against are considered eligible for appraisal rights. SEKIGUCHI, supra note 11, at 437. IMAI ET AL., supra note 31, at 312 (referring to mergers). Many Japanese companies limit possible proxies to other shareholders of the company. Courts have upheld such charter provisions as protecting the company against non-shareholders disturbing the shareholder meeting. KAWAMOTO ET AL., supra note 6, at no. 406.

37 Art. 21-3 Law on Special Exceptions to the Commercial Code concerning Audit, etc., of Stock Companies (Kabushiki kaisha no kansa-tô ni kansuru shôhô no to kurei ni kansuru hôritsu), Law No. 22/1974, as amended by Law No. 80/2001.

38 MAEDA, supra note 22, at no. 297.


40 Id., at no. 4.

41 SHISHIDO, supra note 11, at § 245-2 no. 7. This principle should hold true even after the introduction of appraisal rights in the case of small-scale transaction, which do not require a vote at all. See supra, at III.3.

42 Id. Non-voting preferred shares are also entitled to vote on any amendment of the charter restricting the transferability of shares (Art. 348 para. 2). This also can give them appraisal rights. SEKIGUCHI, supra note 11, at 436.

43 SHISHIDO, supra note 11, at § 245-2 no. 7. IMAI ET AL., supra note 31, at 315 (referring to mergers).

44 Tokyo District Court, October 11, 1983: 515 Hanrei Taimuzu 159. For the assessment of the fair price for such shares see infra, at V.3.
3. *Request for Appraisal*

As a third step, the shareholder has to request the company in writing, stating the class and number of shares, to repurchase his shares within 20 days after the shareholder meeting.\(^\text{45}\) Otherwise the appraisal right becomes void.\(^\text{46}\) This period is kept short in order to limit the uncertainty in the legal relationship between the dissenting shareholder and the company.\(^\text{47}\)

Only shares held without interruption since the shareholder meeting can be subject to appraisal, not shares acquired only after the shareholder resolution.\(^\text{48}\) The shareholder may exercise the appraisal right with regard only to a part of the shares, *e.g.*, in order to adjust his investment under the new circumstances to his risk-preferences.\(^\text{49}\)

4. *Modified Procedure in the Case of Small-Scale Transactions*

Obviously, this procedure has to be modified for small-scale transactions, which do not require shareholder approval but in most cases nevertheless give rise to appraisal rights. To give shareholders the opportunity to exercise their appraisal rights even without a pivotal shareholder meeting, the company has to give public notice\(^\text{50}\) of the proposed transaction or to inform all shareholders individually\(^\text{51}\) within two weeks after the day of the signing of the transaction agreement.\(^\text{52}\) Failing to do so constitutes an offense and can be punished with a fine of up to 1 million Yen (Art. 498 para. 1 no. 2).

The kind of information, which is to be made available, varies slightly by the various forms of small-scale transaction. In the event of a takeover of business the company has to disclose the trade name and the seat of the principal office of the other company, the fact that the transaction will be performed without a shareholder vote and the “essential elements” (*yôryô*) of the takeover. In contrast, for mergers, exchanges, and splits for absorption, the respective provisions on disclosure do not mention these essential ele-

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45 Art. 245-3 (business transfer), which applies also to other transactions. It is necessary that the request actually reach the company within this period (Art. 97 Civil Code).

46 Art. 245-4.

47 SHISHIDO, *supra* note 11, at § 245-3 no. 1.


49 SHISHIDO, *supra* note 11, at § 245-3 no. 1.

50 Public notice is to be given in the Official Gazette or a daily newspaper as specified in the charter (Art. 166 para. 1 no. 9, para. 3).

51 If the company chooses this alternative, it has to inform all shareholders registered in the shareholders record (*kabunushi meibo*). If the company participates in a securities custody and transfer system (*kabuken hokan furikae seido*), this refers to the beneficial shareholder. MAEDA, *supra* note 21, at no. 717-7.

52 Art. 245-5 para. 2 (small-scale takeover of business), Art. 358 para. 4 (small-scale share exchange), Art. 374-23 para. 4 (small-scale split for absorption), Art. 413-3 para. 4 (small-scale merger).
ments. However, in the latter cases the transaction agreement and the other important documents are to be kept at the principal office of the company and can be inspected by the shareholders from the first day the company gives public notice or informs shareholders individually. Thus at least in principle, the shareholders are given the opportunity to make an informed decision in all cases.

From the time of such public notice or individual information onwards, dissenting shareholders have two weeks to send their written objection to the company. An additional limit to small-scale transactions is that a company may not use the facilitated procedure if shareholders representing 1/6 of all voting rights or more have sent such written objection to the company. This figure is identical with the minimum of voting rights required to block the transaction if a vote were taken. If the facilitated transaction cannot be continued for this reason, there are also no appraisal rights. After the two-weeks period following the public notice or individual information has expired, dissenting shareholders have an additional 20 days to request the appraisal of their shares in writing, stating the number and class of their shares. The shareholder has to be registered in the shareholder register at the time he makes this request.

5. Effect of Appraisal Procedure

By unilaterally exercising his appraisal right the shareholder gives rise to a sales contract between himself and the company. The shareholder now owes a duty to transfer the shares specified in the appraisal request, and the company is obliged to pay a purchase

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53 See the provisions listed in the preceding footnote.
54 Art. 374-23 para. 9, Art. 374-18 para. 1 (split for absorption), Art. 358 para. 9, Art. 354 para. 1 (share exchange), Art. 413-3 para. 9, Art. 408-2 (merger).
55 Art. 245-5 para. 3 (takeover of business), Art. 358 para. 5 (share exchange), Art. 374-23 para. 5 (split for absorption), Art. 413-3 para. 5 (merger).
56 Art. 245-5 para. 6 (takeover of business), Art. 358 para. 8 (share exchange), Art. 374-23 para. 8 (split for absorption), Art. 413-3 para. 8 (merger). The written objections received by the company have to be filed when the transaction is registered to prove that the requirement is met (Art. 90 no. 9 Corporate Registration Act (Shōgyō tôki hô); Law No.125/1963, as amended by Law. No. 80/2001). MAEDA, supra note 22, at no. 717-5.
57 A resolution to amend the charter requires a 2/3 majority of the voting rights present representing 1/2 of the total voting rights (Art. 343): 1/2 x 1/3 = 1/6. Assuming the quorum is just met, 1/2 x 1/3 = 1/6 is the minimum to block the transaction. KAWAMOTO ET AL., supra note 6, at no. 584. MAEDA, supra note 22, at no. 717-5. It should be added that in fact one more share is needed.
58 Art. 245-4 (takeover of business), referred to by Art. 349 para. 2 (share exchange), Art. 374-23 para. 7 (split for absorption) and Art. 413-3 para. 7 (merger).
59 Art. 245-5 para. 4 (takeover of business), Art. 358 para. 6 (share exchange), Art. 374-23 para. 6 (split for absorption), Art. 413-3 para. 6 (merger).
60 In the case of a securities custody and transfer system a shareholder can request appraisal after withdrawing his shares from his account and having them registered in his own name. MAEDA, supra note 22, at no. 717-7.
61 Supreme Court, March 1, 1973: 27 Minshû no. 2 161, 167.
price. Until the shares are actually transferred in exchange for the purchase price the shareholder remains a shareholder and may continue to exercise his shareholder rights. If the company abandons the transaction for whatever reason prior to the exchange the appraisal right is voided (Art. 245-4), as there is no need any more to protect the shareholder in that event.

Traditionally Japanese corporate law has been hostile as to acquisitions of a company’s own shares. Until 2001 it allowed share repurchases only in specified cases and up to certain numerical limits (Art. 210 through 211-2 old version). One of these exceptional cases was the acquisition in connection with the execution of appraisal rights (Art. 210 no. 4 old version). However, the company had to dispose of the acquired shares in due time (Art. 211 old version). These provisions mirrored the tensions between the concept of appraisal rights on the one hand and the principle of capital maintenance in the legal capital system on the other, which aims at protecting the creditors of the company. As mentioned before, these frictions gave rise to criticism when appraisal rights first were introduced into Japanese law. Recently the rules on the repurchase of shares have been considerably liberalized in order to enable Japanese companies to make effective use of treasury stocks (kinko kabu) following US models. Thus the historical frictions are eased and another step away from the strict application of the principles of the legal capital system has been accomplished.

If the company and the dissenting shareholder agree on a purchase price for the shares, the company has to pay the agreed amount within 90 days following the resolution adopting the transaction (Art. 245-3). It is not considered a violation of the equal treatment principle, if some shareholders receive higher prices for their shares

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62 As the consent of the company is not required, Japanese legal doctrine categorizes the appraisal right as a so-called keisei-ken, i.e. a right to influence a legal relationship by unilateral declaration. SHISHIDO, supra note 11, at § 245-2 no. 3.
63 Art. 245-3 para. 5.
64 SHISHIDO, supra note 11, at § 245-4 no. 1.
65 See supra, at II.
67 Regarding the fundamental link between the principle of capital maintenance and the ban on share repurchases see MAEDA, supra note 22, at no. 178-10.
68 Incorrect IMAI ET AL., supra note 31, at 316: 90 days from the agreement between the shareholder and the company.
69 The Commercial Code does not expressly state when this period begins for small-scale transactions not requiring a shareholder resolution. It seems reasonable to let the period begin at the end of the 20 days period for objecting the transaction. K. TAKEI/M. HIRABAYASHI, Kaisha bunkatsu no jitsumu [The Practice of Corporate Splits] 72 (2000) (referring to corporate split).
than others. However, an unreasonably high price can be attacked by creditors or give rise to personal liability of the board members.\(^70\)

Not surprisingly, the dissenting shareholder and the company often do not agree on what would constitute a fair price.\(^71\) In case no agreement has been reached at the time 60 days have passed since the adoption of the resolution, the dissenting shareholder may request the court at the principal office of the company to assess the price within an additional 30 days.\(^72\) The company is to pay interest at the statutory rate\(^73\) on any fair value determined by the court starting 90 days after the resolution (Art. 245-3 para. 4 CC, Art. 404 Civil Code). According to the majority of legal scholars the dissenting shareholder keeps his shareholder rights including the right to vote, the right to receive dividends and the right to be allotted new shares until the purchase price is paid.\(^74\) The decision of the court can be appealed subject to a time limit.\(^75\)

6. \textit{Costs}

The procedure described so far, though somehow complicated at first glance, does not demand much more from dissenting shareholders than to stay informed about the development of the corporations and keep track with the various time limits. Small shareholders generally will shy away from this burden. However, on the whole the transaction costs for minority shareholders do not appear to be unreasonable high. Thus appraisal rights seem to be an effective safety valve in the event of a grossly unfair transaction.

The picture looks different if the costs of the court procedure are included. Court costs can be considerably high especially as assessing the fair value of the dissenting shareholders’ stock often will require a professional appraiser to assist the court. According to the applicable rules regarding costs in non-contentious matters,\(^76\) the person filing the request bears the entire court costs. This means, even if the court assesses fair value as requested by the dissenting shareholder, the latter will have to deduct from the granted amount not only his own legal fees, but also the entire court costs. Together with the aforementioned steps, which have to be taken prior to any court request, and

\(^{70}\) SHISHIDO, supra note 11, at § 245-3 no. 3.

\(^{71}\) IMAI ET AL., supra note 31, at 317 (referring to mergers).


\(^{73}\) The statutory rate for commercial transactions is applied, which is 6% per year (Art. 514).

\(^{74}\) IMAI, supra note 39, at § 408-3 no. 17. Some argue, however, that the amount of interests due should be diminished by the amount of dividends paid. SHISHIDO, supra note 11, at 245-3 no. 8.

\(^{75}\) Artt. 132-7, 129-4 Law on Procedures in Non-Contentious Matters.

\(^{76}\) Art. 26 Law on Procedures in Non-Contentious Matters.
the high degree of uncertainty with regard to the result this cost rule seems to have a
deterring effect, which considerably diminishes the practical effectiveness of appraisal
rights.\textsuperscript{77} This is true both for an actual court procedure as well as with regard to an out-
of-court settlement, where the value of appraisal rights as a bargaining chip heavily
depends on the practicability of the dissenting shareholder’s alternative to go to court.

The issue of shareholder protection rules, which are rendered ineffective due to pro-
cedural hurdles, sounds familiar from the derivative suit discussion. Though provided
for by the Commercial Code since 1950, derivative suits only became frequent after the
cost burden had been considerably reduced in 1993.\textsuperscript{78} If appraisal rights are really to
become an effective investor protection instrument, then the Japanese legislator should
reconsider the applicable cost rule. Without legisatory change courts will hardly be
willing to decide on the costs according to the principles of fairness, as some legal
scholars have proposed.\textsuperscript{79} While imposing the entire costs on the company in all cases
might give rise to frivolous claims brought by the infamous shareholder racketeers
(sôkaiya), distributing court costs according to the outcome of the court procedure
seems not only fairer, but also would create the right incentives.

V. VALUING THE MINORITY SHARE

1. General Remarks

Obviously one of the most decisive and at the same time intricate questions concerning
appraisal rights is how courts should assess the value of the dissenting shareholders’
minority shares. While the Law of Procedures in Non-Contentious Matters regulates the
jurisdiction and formal procedure, as to the determination of the price the Commercial
Code only states that the shareholder is entitled to receive for his shares “the fair value
they would have, if the resolution [on the transaction] had not been adopted”.\textsuperscript{80} In the
case of a small-scale transaction performed without a shareholder resolution the share-
holder is entitled to the fair value the shares would have if the company had not entered
into the transaction agreement.\textsuperscript{81}

\textsuperscript{77} See Y. KIMATA, Kabushiki kaitori seikyû tetsuzuki no sai-kentô [Shareholder Appraisal Pro-

\textsuperscript{78} See WEST, supra note 1, at 352. KLIESOW, supra note 1, at 131. It should be noted that
Prof. West’s study casts considerable doubt on whether the reform of the shareholder deri-
native suit mechanism in Japan actually has benefited shareholders, and not rather attorneys.

\textsuperscript{79} SHISHIDO, supra note 11, at § 245-3 no. 6.

\textsuperscript{80} Shônin no ketsugi nakariseba sono yû subekarishi kôsei naru kagaku. Art. 245-2 (transfer
of business, etc.), Art. 355 (share exchange and share transfer), Art. 374-3 (split) and
Art. 408-3 para. 1 (merger).

\textsuperscript{81} Similar provisions are found in Art. 245-5 para. 3 (takeover of business), Art. 358 para. 5
share exchange), Art. 374-23 para. 5 (split for absorption), and Art. 413-3 para. 5 (merger).
Generally, it is assumed that fair value means some kind of going concern value, not the dissolution value. The Supreme Court has held that the courts should determine fair value on a case-by-case basis without being bound by the arguments and the evidence presented by the parties considering ex officio all circumstances. This approach obviously gives the courts much leeway. On the other hand, it is hard to avoid the impression that dissenting shareholders as well as companies are virtually left in the dark about which standard will be applied and what the result will be.

It should be noted that there are various other situations where the problem of how to assess the fair value of shares arises, e.g., the issuance of new shares to third parties (Art. 280-2 para. 2). However it is not undisputable whether there should be one uniform standard or different standards as there are different aims of the valuation in each respective circumstance.

2. **Non-Listed Shares**

Determining fair value is at its most difficult and at the same time most important in the case of non-listed shares, which the dissenting shareholder cannot dispose of at will into a liquid market. Case law in this field is rather sparse and has not developed a general valuation method. Courts have either primarily looked at the assets of the company, or combined factors like net asset value, earning power and a comparison with the market capitalization of similar listed companies in the same line of business. As there seem to have been no cases since the 1980s it is unclear whether today courts would accept a cash flow analysis as valuation method.

While other countries have not yet developed a perfect solution for assessing fair value either, it is fair to say that in Japan the outcome of appraisal procedures in the case of non-listed shares is virtually impossible to predict.

3. **Listed Shares**

Interestingly enough quite a few of the published cases concern appraisal requests for listed stock. At least as long as there is sufficient trading, the stock market price is...
considered to be the predominant, albeit not the only criterion for determining fair value.\(^8^9\) From the language of the law one can infer that the shareholder is not to suffer in case the share price drops due to the adoption of the resolution (respectively in the case of small case transactions the entering into the transaction agreement).\(^9^0\) Thus appraisal rights can in principle be of advantage for dissenting shareholders of a listed company, if the market has reacted negatively to the adoption of the shareholder resolution. Similarly, most commentators seem to agree that in the reverse case, if the stock price goes up due to the approval of the transaction, \(e.g.,\) because the market expects synergies from a merger, dissenting shareholders should not be allowed to participate in such increase in market value.\(^9^1\)

As far as the stock market price is used as prima facie evidence, the question arises the price at which point of time the court should look at. The wording of the statute “if the resolution had not been adopted” cannot be read as meaning the day before the shareholder meeting, as by this time the market will long have reacted to the announced transaction. The courts usually look at the average share price over a certain period before the announcement of the transaction, in order to exclude speculative effects.\(^9^2\) Nevertheless, a clever dissenting shareholder should be able to avoid any market risk during the period between the announcement of the transaction and the appraisal request, as he can abandon the appraisal request, if the market reacts positively to the announcement, or in the opposite case, can ask for appraisal calculated on the average stock price before the announcement. If the dissenting shareholder has acquired the shares only \(a f t e r\) the transaction had been announced, courts have held that the assessed value cannot exceed the purchase price even if the shares traded higher prior to the announcement of the transaction.\(^9^3\)

\(^8^9\) Hanrei Taimuzu 159, appealed in High Court Tokyo, December 14, 1983: 525 Hanrei Taimuzu 285. These cases all refer to mergers.

\(^9^0\) District Court Yokohama, January 21, 1972: 666 Hanrei Jihô 91, 92 (considering also the earning power and the assets of the company as well as the proposed exchange ratio of the merger). SHISHIDO, supra note 11, at § 245-2 no. 12. IMAI ET AL., supra note 31, at 316.

\(^9^1\) SHISHIDO, supra note 11, at § 245-2 no. 13.

\(^9^2\) District Court Yokohama, January 21, 1972: 666 Hanrei Jihô 91, 92; District Court Tokyo, February 10, 1983: 1068 Hanrei Jihô 110, 111. In the latter case the dissenting shareholder had requested appraisal at the market price two days before the announcement of the merger, which due to alleged speculative effects was 2620 Yen / share. Considering the development of the stock within the last 6 months before the announcement of the merger, the court granted only 1861 Yen / share. The company had entered into negotiations offering 1353 Yen / share, later raising its offer to 1727 Yen / share.

\(^9^3\) District Court Tokyo, October 11, 1983: 515 Hanrei Taimuzu 159, 160. The second instance refused to view this as a violation of the principle of equal treatment of all shareholders. High Court Tokyo, December 14, 1983: 525 Hanrei Taimuzu 285, 286.
VI. NO EXCLUSIVITY OF THE APPRAISAL REMEDY

According to the majority of Japanese legal scholars there is no exclusivity of the appraisal remedy.\(^\text{94}\) A shareholder therefore has the choice whether to opt for appraisal or to bring a suit in order to have the transaction be declared void by the court.\(^\text{95}\) It is assumed that a shareholder may file a suit seeking the resolution to be set aside or declared void by the court, and at the same time (based on the validity of the resolution) enter into appraisal proceedings to be appraised if the court dismisses the claim.\(^\text{96}\) If, however, the suit is successful before the purchase price for the shares is paid, the appraisal right becomes void. If the purchase price is paid while the suit is pending, the claim is dismissed as the plaintiff is no longer a shareholder and thus has no longer a standing for such suit.\(^\text{97}\)

Courts have held that a grossly unfair exchange ratio as such cannot constitute a reason to declare a merger void, as dissenting shareholders have the right to request appraisal.\(^\text{98}\) However, it is assumed that in the case of a conflict transaction, the court can set aside the resolution or void the transaction, if the resolution has been adopted with the votes of the interested shareholder (Artt. 247, 415).\(^\text{99}\) Some authors argue that the appraisal right should not be considered to bar a suit to void the transaction, as otherwise the shareholder would be left with the choice to either give in or to request appraisal and leave the company.\(^\text{100}\)

Theoretically, a shareholder in the case of an unfair transaction could also sue the directors for damages. However, in order to succeed he would have to establish bad faith or gross negligence (Art. 266-3). There seem to be no cases, in which dissenting shareholders have actually pursued this option.

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\(^{95}\) The Commercial Code provides for special forms of suits seeking the nullification of share exchanges (Art. 363), share transfers (Art. 372), corporate splits (Art. 374-12 and 374-28) and mergers (Art. 415) after the respective transaction has taken effect. Until then the shareholder can file an injunction (Art. 272) or bring a general suit in order to have the resolution be set aside (Art. 247) or declared void (Art. 252).


\(^{97}\) SEKIGUCHI, supra note 11, at 440.

\(^{98}\) District Court Tokyo, August 24, 1989: 1331 Hanrei Jihô 136, 139. Mitsui Bussan had merged its 85% subsidiary into itself forcing the minority shareholders of the subsidiary to accept one share in the company for each share in the subsidiary. One shareholder requested the court to declare the merger void according to Art. 415, alleging the exchange ratio was grossly unfair. The merger on part of the subsidiary had been approved with the votes of Mitsui Bussan. The court dismissed the claim leaving the question open, whether a conflict transaction was given, as it considered the exchange ratio to be fair.


\(^{100}\) TATSUTA, supra note 96, at no. 111.41.
VII. COMPARISON WITH AMERICAN MODELS

As mentioned above, the number of Japanese court decisions on appraisal is fairly limited and does not allow drawing meaningful conclusions. We do not know how many cases settle and whether the cases, which are finally decided by the court, are typical of all appraisal proceedings. Nor is there any record on the results of the settlement negotiations. What we do know, however, is that the parties negotiate in the shadow of the law and that the dissenting shareholder at least on the margin will only achieve a favorable result to the extent the law provides him with rights and enables him to actually pursue these rights in court, if no settlement is reached. Therefore, the law indirectly will determine the outcome of the cases, which are settled, as well.

To evaluate the effectiveness of the appraisal remedy in Japanese law, its substantive and procedural rules on appraisal, therefore, shall be contrasted with the respective models known from the US. For reasons of simplicity, out of the great variety of appraisal rules in the various states, the comparison will be limited to the appraisal rules of the Delaware General Corporation Law (DGCL) as the dominant corporate law in the US and the Revised Model Business Corporation Act of 1999 (RMBCA) as the most recent model law in the field. Both statutes are among the more restrictive provisions in the US.

1. Scope of Application

With regard to the scope of application, Japanese law seems to be more generous to dissenting shareholders than the DGCL and the RMBCA. Shareholders in Japan are entitled to receive appraisal if the company performs a business transfer (Art. 245-2, business transfer). By contrast, the Delaware statute does not provide shareholders with appraisal rights in the event of an asset deal. Even if the transaction is artificially designed as asset deal in order to deprive minority shareholders of their appraisal remedy, the courts have refused to grant appraisal rights based on a de-facto merger doctrine.\(^\text{101}\)

Furthermore, Japanese law grants appraisal rights to minority shareholders in the event of most small-scale transactions.\(^\text{102}\) If shareholders are not allowed to vote on a merger in Delaware according to the “whale swallows minnow” exception, they also do not have appraisal rights (DGCL §§ 252(f), 262(b)(1)(ii)). The same is true with regard to small-scale mergers and small-scale share exchanges under the RMBCA (§§ 11.04, 13.02(a)(1)).

The Japanese Commercial Code provides for appraisal rights even if the company is listed at the stock exchange. There is no market-out exception as in DGCL § 262(a)(1) or RMBCA § 13.02(b)(1)(i). One might suspect that including listed shares does not make a big difference in practice, as most shareholders will choose the uncomplicated exit via


\(^{102}\) See supra, at III.3.
the stock market. However, among the few court decisions on appraisal rights there are a surprising number of cases involving listed shares.\footnote{See cases listed supra, at note 89.}

In two more respects the RMBCA is more restrictive than the Japanese Commercial Code: Firstly, shareholders of the surviving company in a merger whose shares remain outstanding are not entitled to appraisal rights (RMKBCA § 13.02 (a)(1)). Secondly the charter may eliminate appraisal rights for preferred shares (RMBCA § 13.02(c)).

2. Procedure of Appraisal

With regard to the scope of application shareholders can be quite satisfied with the Japanese rules. The procedural rules at least of the RMBCA, however, appear to be far superior nourishing the suspicion that the Japanese legislator has provided many rights, which prove scarcely effective in practice. In the US as well as in Japan a dissenting shareholder has to go through various steps, a burden few retail shareholders will take upon them. However, while it can take a long time in Delaware as well as in Japan until the court decision is rendered, the RMBCA has made remarkable efforts to get funds into the hands of the shareholder at an early stage. The company is compelled to pay the shareholder cash equivalent to the corporation’s estimation after the shareholder has made a second request following the shareholder meeting (RMBCA § 13.24). This should also considerably shift the balance of power in negotiations about the remaining difference.

In addition, RMBCA § 13.31 allows the court to impose attorney and expert fees on the company. Thus the RMBCA removes a major barrier, which seems to be almost insurmountably high in Japan. Such step should not increase the risk of abuses, if like under the RMBCA rule, the court has the power to impose the costs on the shareholder whenever the suit is frivolous. Alternatively the costs could be distributed according to the outcome of the case measured against the last offer of each side in prior negotiations.

Finally, the valuation of the dissenting shareholders’ stock seems to be at least slightly more predictable in US courts than in Japan. Even if the Delaware block method has been abandoned in favor of more flexible valuation methods,\footnote{Weinberger v. UOP, 457 A.2d 701(Del. Supr. 1983).} a dissenting shareholder still should be better able to make a judgment about the appraisal amount to expect than in Japan, where courts so far have failed to establish any consistent standard.
VIII. CONCLUSION

Since first introduced into the Japanese Commercial Code in 1950 additional appraisal rights provisions have been a consequence of a remarkable number of legislative innovations. Especially since the deregulation of Japanese corporate law gained impetus in the 1990s, the legislator has repeatedly broadened the scope of appraisal rights to new forms of transaction, in order to strike the right balance between the interests of majority shareholders and minority shareholders.

Nevertheless, a close look at the Japanese appraisal rules reveals serious doubts about the effectiveness of the appraisal remedy in Japan. This suggests that it might have been premature to credit Japan with strong investor protection by pointing to the mere existence of appraisal rights.\textsuperscript{105} The virtual unpredictability of the result of an appraisal proceeding in a Japanese court combined with the heavy cost burden seem to impede the achievement of effective minority shareholder protection considerably. It must be assumed that this not only deters shareholders from going to court, but also puts them into a weak bargaining position for out-of-court settlements.

As mentioned at the outset the results of this article can only be preliminary as long as empirical data are virtually non-existent. Furthermore, a comprehensive comparative evaluation would have to more closely consider complementary alternative mechanisms of minority shareholder protection in Japan, as well as structural weaknesses in the appraisal proceedings in other countries. If future research, however, confirms the findings of this article the Japanese legislator should consider removing the aforesaid barriers to transform appraisal rights in Japanese corporate law into the effective remedy they are supposed to be. This might enable Japan to better reap the benefits of strong minority shareholder protection, among them large capital markets and improved corporate governance.\textsuperscript{106}

\textsuperscript{105} I am therefore inclined to agree with IGARASHI, \textit{supra} note 5, at 96 that there must be something that the works of LA PORTA ET AL. have not captured.

\textsuperscript{106} LA PORTA ET AL., Investor Protection, \textit{supra} note 4, at 16 \textit{et seq.}
allein die Tatsache der gesetzlichen Statuierung solcher Rechte noch nicht automatisch auch einen effektiven Schutz in der Praxis bedeute.


(die Red.)