

METI Expanded Scope of Industries Subject to Prior Notification for Foreign Direct Investment

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Authors: [Jun Usami](#), [William Moran](#), [Shino Asayama](#), [Kei Horiguchi](#), [Naoto Nelson Saika](#)

On May 27, 2019, the Ministry of Economy, Trade and Industry of Japan (METI) expanded the scope of the industries for which submission of a prior notification is required for foreign direct investment. This recent revision of relevant rules in Japan reflects METI's increasing attention to cybersecurity and leakage of emerging technologies and calls for foreign investors' careful review of their investments into Japan as to whether the subject industry falls within the expanded scope of the requirement and thereby submission of a prior notification is required.

Expansion of Scope of Industries Subject to Prior Notification Requirement

METI's public notice dated May 27, 2019 revised relevant Cabinet orders pursuant to Articles 27.1 and 28.1 of the Foreign Exchange and Foreign Trade Act of Japan and expanded the scope of industries that are subject to the prior notification requirement for foreign direct investment to include industries of advanced technologies. We provide an overview of the expanded scope and implications thereof below.

Overview of Prior Notification Requirement

Foreign Exchange and Foreign Trade Act of Japan requires that a foreign investor submit a prior notification to, and receive approval from, the Minister of Finance and other minister(s) having jurisdiction over the pertaining business in a case in which a foreign direct investment (specifically, inter alia, those that result in acquiring shares of an unlisted company or more than 10% of shares of a listed company) is made to a Japanese company in a certain industry that is subject to the prior notification requirement due to, inter alia, security concerns.

In particular, the following industries have been subject to the prior notification requirement under the relevant rules before the revision:

- Industries relevant to "national security" — manufacturing industries pertaining to ammunition, aircrafts, nuclear power, and space development, and industries manufacturing general articles with a high probability of diversion to military use;
- Industries relevant to "public order" — industries pertaining to electric power, gas, heat supply, telecommunication, broadcasting, water supply, railway, and passenger transportation;

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- Industries relevant to “public safety” — industries manufacturing biological preparations and security service industry; and
 - Industries relevant to the smooth management of the Japanese economy — industries pertaining to agriculture, forestry, fishery, petroleum, hide and leather goods, air transportation, and ocean shipping.

Overview of Revisions

According to the government press release, the expansion of the scope of the industries subject to the prior notification requirement was due to “recent increasing importance of cybersecurity and prevention of situations causing significant adverse effects, such as leakage of highly-important technology for the purpose of national security and damages to bases of defense production and defense technology. With the revision of the rules, (A) additional industries will become subject to the prior notification requirement, and (B) the scope of the industries currently subject to the prior notification requirement will be expanded to cover more business entities.

Additional Industries Subject to Prior Notification Requirement

The following industries will become subject to the prior notification requirement.

(1) Industries Manufacturing Information Processing Devices and Parts Thereof

This category includes industries manufacturing the following products:

- integrated circuits,
- semiconductor memory media,
- optical disks, magnetic discs, and magnetic tapes,
- electronic circuit boards,
- wired communication devices,
- mobile phones,
- radio communication devices,
- electronic computers,
- personal computers, and
- external memory devices.

(2) Industries Pertaining to Software for Information Processing

This category includes industries pertaining to the following businesses:

- customized development of software,
- development of embedded software, and
- development of packaged software

(3) Industries Pertaining to Information Communication Service

This category includes industries pertaining to the following businesses:

- wired broadcast and telephone services, and
- information processing services

Expanded Industries Subject to Prior Notification Requirement

The scope of industries pertaining to the following businesses will be expanded for the purpose of the prior notification requirement:

- regional telecommunication services,
- long distance telecommunication services,
- other landline telecommunication services,
- mobile telecommunication services, and
- services supporting internet access.

In short, with this scope expansion, the business entities that are not required to register as telecommunication carriers under Article 9 of Telecommunications Business Act will become subject to the prior notification requirement. In particular, telecommunication service suppliers that do not have their own telecommunication facilities (e.g., servers and base stations) – for example, those that provide services through third parties' cloud servers and/or other companies' communication network – will be required to submit prior notifications.

It appears that this scope expansion covers low-cost mobile telecommunication services, which are becoming popular in Japan.

Background and Implication

As mentioned above, increasing cybersecurity risks and concerns of leakage of advanced technologies (including technologies for artificial intelligence, or AI) were major factors behind this revision of rules. This intention of METI appears to have been reflected in the fact that industries pertaining to hardware (e.g., integrated circuits) and embedded software, which are essential for application of AI technologies, have been added to the scope of the requirement. It suggests that METI intends to have generally all industries pertaining to AI developments be subject to the prior notification requirement. Including various types of communication services in the scope of the requirement appears to be METI's attempt to enhance cybersecurity.

This revision of rules did not adopt a holistic definition of relevant concepts such as “emerging technologies” provided in CFIUS. It, however, practically covers all the relevant industries of emerging technologies – with respect to AI technologies, for example, industries pertaining to integrated circuits, embedded software, and customized software development will fall within the scope of the requirement – and thereby addresses the concerns of leakage of emerging technologies.

Transitional Measure

The revised rules will be implemented and enter into effect on August 1, 2019. Prior notification will not be required for the expanded scope if the foreign investment will be made before August 31, 2019. If the foreign investment will be made on or after August 31, 2019, the foreign investor will be required to submit a prior notification on or after August 1, 2019.

White & Case LLP
White & Case Law Offices
(Registered Association)
Marunouchi Trust Tower Main
26th Floor, 1-8-3 Marunouchi
Chiyoda-ku, Tokyo 100-0005
Japan

T +81 3 6384 3300

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