

Japan Regulatory Update

Japan

DT Legal Japan

December 7, 2017

Revisiting the Article 63 Exemption at the end of 2017

A. Background

This Client Alert is intended for fund managers currently operating under the “Exemption for Special Business Activities directed at Qualified Institutional Investors” pursuant to Article 63 of the Financial Instruments and Exchange Act of Japan (the “**Article 63 Exemption**”). As 2017 comes to a close, we believe that general partners operating under the Article 63 Exemption (“**Article 63 Exemption Operators**”) should assess their Japan activities to confirm whether they need to continue to operate under the Article 63 Exemption.

We view this confirmation to be particularly relevant at this time as those Article 63 Exemption Operators who are still operating under the Article 63 Exemption as of the end of the current fiscal year (i.e. December 31, 2017 for many of the Article 63 Exemption Operators) will be required to file an annual business report (*jigyō houkokusho*, “**Annual Business Report**”) to the Kanto Local Finance Bureau in relation to each relevant limited partnership fund (“**LP Fund**”) within three months, in principle, after the end of the fiscal year. Given that the Article 63 Exemption Operator will be required to disclose various information (including certain financial statements) in its Annual Business Report and the fact that the Annual Business Report will be available to the public¹, we recommend that each Article 63 Exemption Operator uses this opportunity to assess whether they need to continue to operate as an Article 63 Exemption Operator.

This Client Alert will provide a brief summary of the analysis required for Article 63 Exemption Operators for this determination.

B. Analysis

For the purposes of this determination, it is necessary to recall that the Article 63 Exemption is an exemption with respect to two specific registered business activities: (i) self-marketing activities; and (ii) self-management activities.

(i) Self-Marketing.

Article 63 Exemption Operators are permitted to engage in self-marketing to Japan investors of the interests in the relevant LP Fund without being registered as, or appointing, a registered Type 2 Financial Instruments Dealer. If the Article 63 Exemption Operator is currently not engaging in any self-marketing activities in Japan (e.g. the LP Fund is closed), it will not need to rely on this aspect of the Article 63 Exemption.

(ii) Self-Management.

The analysis with respect to “self-management” is slightly more difficult. As a matter of default, with respect to a LP Fund, each general partner is deemed to be engaging in “self-management” to each of the Japanese limited partners and would therefore be required to be registered to engage in an investment management business in Japan (an “**Investment Manager**”).² However, as it is practically impossible for a general partner to register as an Investment Manager, general

¹ Similar to the Article 63 Notification, the Annual Business Report of the Article 63 Exemption Operator must be made available to the public of Japan – though certain information may be redacted.

² If the general partner is delegating investment management authority to an Investment Manager registered in Japan, such general partner will not be deemed as engaging in “self-management”.

partners may rely on the Article 63 Exemption to exempt itself from foregoing requirement to register as an Investment Manager.

However, there are two notable exemptions to the above requirement for a general partner to register as an Investment Manager:

(a) The De Minimis Exemption³

If the relevant LP Fund satisfies all of the following requirements (on a per fund basis):

1. the number of the Japanese investors⁴ in the relevant LP Fund is less than ten (10);
2. each of the Japanese investors⁵ are a Qualified Institutional Investor or registered as an Article 63 Exemption Operator;⁶ and
3. the total contributions made by the direct Japanese investors are no more than one-third (1/3) of the total contributions made by all of the limited partners of the relevant LP Fund.

(b) The Article 61, Paragraph 3 Exemption

If all of the Japanese investors are either Investment Managers or registered financial institutions engaging in investment management business, the general partner will not be deemed to be engaging in self-management with respect to such Japanese limited partners.

Based on the descriptions set forth above, we recommend that Article 63 Exemption Operators examine the profile of the Japanese investors in their LP Fund and make a determination as to whether it is still necessary to operate under the Article 63 Exemption.⁷

C. Next Steps

After completing the determination above, if the Article 63 Exemption Operator is no longer engaging in both: (i) self-marketing activities; and (ii) self-management activities, we suggest that such Article 63 Exemption Operator seeks to de-

register itself from the Article 63 Exemption. The de-registration process for Article 63 Exemption Operators is quite simple and can be typically completed within one week.

For those Article 63 Exemption Operators who will need to continue to rely on the Article 63 Exemption, it will be necessary to prepare and submit its Annual Business Report by the end of March 2018.

The Investment Management Group of DT Legal is happy to assist Article 63 Exemption Operators to de-register from the Article 63 Exemption, or, as necessary, assist in the preparation of the Annual Business Report.

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³ Article 16, Paragraph 1, Item 13 of the Cabinet Office Ordinance regarding Definitions under Article 2 of the Financial Instruments and Exchange Act (the "Definitions Ordinance").

⁴ Including both direct Japanese investors and indirect Japanese investors which have subscribed through a Japan limited partnership.

⁵ Including both direct Japanese investors and indirect Japanese investors which have subscribed through a Japan limited partnership.

⁶ As defined under Article 2, Paragraph 3, Item 1 of the Financial Instruments and Exchange Act of Japan and Article 10 of the Definitions Ordinance.

⁷ It should be noted that while this Client Alert is intended as a summary of the relevant analysis, we would recommend confirmation with Japan counsel as to the specific determination.

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Contacts

DT Legal Japan (Tokyo)

Koji Yamamoto, Partner

koji.yamamoto@tohmatu.co.jp

Yoshiyuki Omori, Partner

yoshiyuki.omori@tohmatu.co.jp

Issued by

DT Legal Japan

Shin-Kokusai Building 2F, 3-4-1 Marunouchi,

Chiyoda-ku, Tokyo 100-0005, Japan

Tel : +81 3 6870 3300

Corporate Info.: www.deloitte.com/jp/en/dtlegal

Investment Management Services:

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