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## **Shareholder Protection in Close Corporations and the Curious Case of Japan: The Enigmatic Past and Present of Withdrawal in a Leading Economy**

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# Shareholder Protection in Close Corporations and the Curious Case of Japan: The Enigmatic Past and Present of Withdrawal in a Leading Economy

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Names of Japanese people mentioned in this Article are given in the Family Name—Personal Name order that is proper in Japanese usage except when citing a Western-language publication authored by a Japanese person. Given the ongoing challenges created by the COVID-19 pandemic for the editorial process such as closure of libraries

**ABSTRACT**

*Oppressed, outvoted, and outgunned, minority shareholders have an obvious solution for their woes: vote with their feet, sell their shares, and leave the company. But this “Wall Street Rule” is only available to shareholders in publicly listed corporations; shareholders in close corporations—privately owned business entities with no market for their shares—do not have the option of easy exit. Legal solutions which enable the shareholder to voluntarily exit a company with their capital such as the oppression or unfair prejudice remedies in US and Anglo-Commonwealth corporate law—what this Article classifies as “withdrawal remedies”—are therefore vital in close corporations.*

*However, until relatively recently, shareholders in Japan’s close corporations had no access to withdrawal under corporate law, as neither of Japan’s then-dominant close corporation forms offered it. By revealing how shareholder litigants, attorneys, and judges in Japan responded to the absence of withdrawal, this Article shows how Japan’s experience was no outlier among nations, but instead powerfully demonstrates the importance of withdrawal remedies in practice. Later, withdrawal remedies at law for close corporations became available in Japan for the first time with the watershed *Kaisha-hō* (Companies Act) of 2005, which introduced a new close corporation form, the *Gōdō Kaisha* (GK). This Article analyzes the challenges facing Japan’s new withdrawal regime and shows how comparative corporate law—armed with the law and experience of withdrawal in the United States, the United Kingdom, and Germany—offers valuable insights for the development of withdrawal in the world’s second largest developed economy.*

Keywords: comparative corporate law, close corporations, shareholder remedies, Japan, withdrawal

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and social distancing, in departure from usual practice, I as the author alone take full responsibility for the accuracy of the non-English-language sources cited and the propositions advanced herein that are based on non-English-language sources.

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## I. INTRODUCTION

Oppressed, outvoted, and outgunned minority shareholders have an obvious solution for their woes: vote with their feet, sell their shares, and leave the company. But this “Wall Street Rule” is only applicable to shareholders in publicly listed corporations. What if selling your shares on the stock market is simply not an option—because there is no market for them? Although the importance of shareholder exit is taken for granted by corporate governance scholars devoted to the study of *public corporations*, exit’s equally essential role in *close corporations*—privately owned business entities for which a market for shares does not exist<sup>1</sup>—is often overlooked. Legal solutions enabling the shareholder to voluntarily exit a company with their capital such as the oppression or unfair prejudice remedies in the United States<sup>2</sup> and Anglo-Commonwealth<sup>3</sup> corporate law—which are defined as

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1. See *infra* Part II.A (describing close corporations).

2. See generally F. HODGE O’NEAL & ROBERT B. THOMPSON, O’NEAL AND THOMPSON’S OPPRESSION OF MINORITY SHAREHOLDERS AND LLC MEMBERS § 7:11 (rev. 2d ed., 2004) (loose-leaf) [hereinafter O’NEAL AND THOMPSON’S OPPRESSION OF MINORITY SHAREHOLDERS] (detailing oppression and unfair prejudice remedies in the United States).

3. The oppression or unfair prejudice remedy has been adopted by jurisdictions including Australia, Canada (federal), Hong Kong, New Zealand, Singapore, and the United Kingdom. For the various statutory regimes, see Corporations Act 2001 (Cth.), §§ 232–35 (Austl.); Canada Business Corporations Act, R.S.C. 1985, c. C-44, §§ 238, 241–

“withdrawal remedies” in this Article<sup>4</sup>—are therefore vital in close corporations. This family of doctrinally distinct but functionally equivalent legal solutions is ubiquitous and well-established in the world’s leading corporate law jurisdictions—the United States, the United Kingdom, and Germany<sup>5</sup>—save one: Japan.

Until relatively recently, shareholders in Japan’s close corporations had no access to withdrawal under the law, as neither of Japan’s then-dominant close corporation forms—the *Kabushiki Kaisha* (KK) (“Stock Corporation”) and the *Yūgen Kaisha* (YK) (“Limited Liability Corporation”)—offered it.<sup>6</sup> This omission attracted little attention in international corporate law literature and was unremedied by both judicial development and statutory reform despite the efforts of Japanese scholars influenced by foreign law models.<sup>7</sup> By revealing how shareholders and other stakeholders in Japan responded to the absence of withdrawal, this Article shows how Japan’s experience powerfully demonstrates the importance of withdrawal remedies in practice.<sup>8</sup>

After decades without withdrawal, in 2005 things changed—but not quite as one might expect. It was not the country’s venerable close corporation forms that finally received long-overdue withdrawal rights; rather, a new close corporation form, the *Gōdō Kaisha* (GK), as introduced by the watershed *Kaisha-hō* (“Companies Act”),<sup>9</sup> came with withdrawal rights. A legislative invention inspired by the American limited liability company (LLC) and with no relationship to the YK, the GK was conceptualized as a third member of a new legal category, the *Mochibun Kaisha* (membership companies), which is separate and distinct from both the KK and YK.<sup>10</sup> The availability of withdrawal in the GK flowed from this quirk of legal classification, rather than as any belated response to earlier serious (but ultimately defeated) reform efforts arising from the problems associated with the lack of withdrawal in the KK and YK, or as any result of inspiration from the

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42 (Can.); Companies Ordinance, (2013) Cap. 622, §§ 723–27 (H.K.); Companies Act 1993, §§ 174–75 (N.Z.); Companies Act (Cap. 50, rev. ed. 2006) § 216 (Sing.); Companies Act 2006, c. 46, §§ 994–96 (U.K.).

4. See *infra* Part II.B (discussing the definition and disambiguation of withdrawal).

5. See *infra* Part II.C (discussing withdrawal remedies in these jurisdictions).

6. See *infra* Part II.A–B (discussing the KK and YK and the absence of withdrawal).

7. See *infra* Part III.C.1–2 (discussing how scholars in Japan perceived the phenomenon of withdrawal’s absence and the failed legislative attempt at introducing withdrawal).

8. This is the goal of Part III.C.

9. *Kaisha-hō* [Companies Act], Law No. 86 of 2005 (Japan). The GK is regulated under its own Part. See *id.* arts. 575–675 (comprising Part III of the *Kaisha-hō*, which regulates the GK).

10. See *infra* Part IV.A.1 (providing background to the GK’s introduction); Part IV.A.2 (defining *mochibun kaisha*).

United States.<sup>11</sup> The advent of the GK presents corporate law jurists with a historic opportunity: a near-blank slate on which conflicts in a new close corporation entity can be solved without the baggage of bad precedent or outdated doctrine. Although Japanese jurists working on the GK have often looked to the United States as a source of inspiration and ideas, this Article offers a different perspective; it argues that withdrawal remedies developed in the United Kingdom and Germany offer greater guidance from a comparative perspective.<sup>12</sup>

This Article proceeds as follows. Part II first introduces the central features of close corporations and the concept of “withdrawal remedies,” and then briefly introduces their operation in the United States, United Kingdom, and Germany. Part III sets out the historical context to Japan’s close corporation law, and proceeds to identify—and offer a nuanced answer to—an unnoticed (in Western literature) but critical puzzle: If withdrawal is essential for close corporations, how did Japanese corporations and shareholders survive without it for so long? Part IV follows with a concise introduction to Japan’s new close corporation form, the GK, highlighting its features and legal significance; some clarifications as to terminology will also be made. Part V is a detailed examination of Japan’s withdrawal regime—the first such analysis in the English language. Part VI takes stock of the GK’s growing importance, and offers comparative insights from the United States, United Kingdom, and Germany for the development of the GK’s withdrawal regime. Notwithstanding the lack of jurisprudence and awareness about the GK’s withdrawal regime and the KK’s continued popularity as a close corporation entity despite the absence of withdrawal, the GK’s ascendance makes withdrawal a rare and valuable opportunity for comparative corporate law jurists to make an impact on close corporation law: the corporate law of the ordinary businessperson.

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11. See *infra* Part IV.A.2 (discussing how withdrawal became a feature of the GK).

12. This argument is developed in Part VI.B below.

## II. WITHDRAWAL REMEDIES AND CLOSE CORPORATIONS: AN OVERVIEW

### A. *Close Corporations: Features and Problems*

Close corporations, like all business corporations, possess standard corporate characteristics, such as separate legal personality (entity shielding) and formal separation at law of share ownership and management power.<sup>13</sup> Although impossible to define with certainty,<sup>14</sup> “close corporations” are associated with specific characteristics, particularly restrictions on shareholder exit and informal management arrangements.

*Restrictions on shareholder exit.* Although equity interests in corporations may be freely transferred,<sup>15</sup> shares of close corporations are typically subject to share transfer restrictions, whether mandatory<sup>16</sup> or as adopted by the company’s constitution.<sup>17</sup> Lack of secondary markets for such shares<sup>18</sup> means that unhappy shareholders do not have the option of following the “Wall Street Rule” and selling their shares on the stock market.<sup>19</sup> Thus, share transfer

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13. REINIER KRAAKMAN, JOHN ARMOUR, PAUL DAVIES, LUCA ENRIQUES, HENRY B. HANSMANN, GÉRARD HERTIG, KLAUS J. HOPT, HIDEKI KANDA & EDWARD B. ROCK, *THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH* 5 (3d ed., Oxford University Press 2017).

14. Robert A. Kessler, *The ABA Close Corporation Statute*, 36 *MERCER L. REV.* 661, 661 (1985) (“[A] close corporation [is] like a spiral staircase: difficult to define, but you know one when you see it.”).

15. KRAAKMAN, ARMOUR, DAVIES, ENRIQUES, HANSMANN, HERTIG, HOPT, KANDA & ROCK, *supra* note 13, at 10.

16. *See, e.g.*, Kaisha-hō [Companies Act], Law No. 86 of 2005, art. 585 (Japan) (prescribing the conditions on which equity interests in membership companies may be transferred).

17. *See, e.g.*, Gesetz betreffend die Gesellschaften mit beschränkter Haftung [GmbHG] [Limited Liabilities Company Act], July 17, 2017, BGBl I at 7, § 15(5) (Ger.) (“The articles of association may stipulate that the transfer of shares be made dependent on further conditions, in particular the company’s consent.”); Kaisha-hō, art. 107(1)(i) (giving stock corporations the option to condition the assignment of shares on approval by the corporation); Companies Act 2006, c. 46, § 544(1) (U.K.) (“The shares or other interest of any member in a company are transferable in accordance with the company’s articles.”).

18. *See, e.g.*, DEL. CODE ANN. tit. 8, § 342(a)(3) (2020) (prohibiting a Delaware statutory “close corporation” from making an “offering of any of its stock of any class which would constitute a ‘public offering’ ”); F. HODGE O’NEAL & ROBERT B. THOMPSON, O’NEAL AND THOMPSON’S CLOSE CORPORATIONS AND LLCs: LAW AND PRACTICE § 1:2 (rev. 3d ed. 2004) (loose-leaf) (noting the lack of a market for minority shareholders’ shares of closely held corporations) [hereinafter O’NEAL AND THOMPSON’S CLOSE CORPORATIONS AND LLCs].

19. Harvey Wells, *The Rise of the Close Corporation and the Making of Corporation Law*, 5 *BERKELEY BUS. L.J.* 263, 275 (2008); GREGOR BACHMANN, HORST EIDENMÜLLER, ANDREAS ENGERT, HOLGER FLEISCHER & WOLFGANG SCHÖN, *REGULATING THE CLOSED CORPORATION* 6–7, 35 (De Gruyter 2014).



restrictions often translate into stable shareholding structures in close corporations with permanent majorities and minorities.<sup>20</sup>

*Informal management arrangements.* Shareholders often participate directly in close corporation management as directors, employees, or both.<sup>21</sup> The absence of clear separation between ownership and control creates organizational and managerial problems distinct from public, widely held corporations. Overlap between management and shareholders and the small number of shareholders in a close corporation aligns the interests of the two classes.<sup>22</sup> Conflicts between directors and shareholders—the dominant agency problem in widely held corporations—are thus rare in close corporations.<sup>23</sup> Instead, the primary problem is conflict between shareholders, particularly majority/controlling versus minority shareholders. Despite advantages associated with the strong personal relationships between co-shareholders,<sup>24</sup> there is a downside: conflicts between shareholders are the “Achilles heel” of the close corporation.<sup>25</sup> Rent-seeking behavior aside, personal conflicts may also spill over into the business realm<sup>26</sup> with potentially devastating consequences for the corporation’s operational health or even its continued existence.<sup>27</sup>

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20. BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 34.

21. See Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV. 271, 273 (1986) (noting that in a close corporation “the firm’s principal investors are also its managers”); Edward B. Rock & Michael L. Wachter, *Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations*, 24 J. CORP. L. 913, 916 (1999) (noting that in close corporations there is “substantial overlap between suppliers of capital and suppliers of labor”).

22. See Easterbrook & Fischel, *supra* note 21, at 273–74 (arguing that agency costs are reduced in a close corporation because the small number of participants facilitates monitoring and because these participants are simultaneously managers and residual risk bearers).

23. BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 8.

24. *Id.* at 31; Easterbrook & Fischel, *supra* note 21, at 274 (describing the advantages of shareholder relationships in close corporations).

25. Mette Neville, *A Statutory Buy-Out Right in SMEs – An Important Corporate Governance Mechanism and Minority Protection?*, in COMPANY LAW AND SMEs 247, 247 (Mette Neville & Karsten Engsig Sørensen eds., Thomson Reuters 2010); see also Sandra K. Miller, *Minority Shareholder Oppression in the Private Company in the European Community: A Comparative Analysis of the German, United Kingdom, and French “Close Corporation Problem”*, 30 CORNELL INT’L L.J. 381, 383 (1997) (“Shareholder disputes present one of the most difficult and potentially destructive problems which arise in the context of the close corporation.”).

26. See Benjamin Means, *A Voice-Based Framework for Evaluating Claims of Minority Shareholder Oppression in the Close Corporation*, 97 GEO. L.J. 1207, 1208 (2009) (observing that “family quarrels and soured friendships often lead to punitive business consequences” in close corporations).

27. O’NEAL AND THOMPSON’S OPPRESSION OF MINORITY SHAREHOLDERS, *supra* note 2, §1:4; see also BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 31.

Shareholder conflicts may arise when the majority and minority disagree on issues such as business direction or fundamental changes such as the sale or restructuring of the business.<sup>28</sup> Other conflict situations include unmet minority expectations on returns or participation in the business; or the exercise of rights or powers by the majority in ways that are abusive or harmful to the minority.<sup>29</sup> Absent special legal rules for the protection of the minority, the result is most often a *fait accompli* in favor of the majority; this is because the principle of majority rule grants majority shareholders substantial control over the majority–minority shareholder relationship.<sup>30</sup>

Not only are minority shareholders vulnerable to majority opportunism, the combination of share transfer restrictions and lack of easy exit options leaves them with few options. Minority shareholders are outvoted by definition and have no legal power to terminate conflicts in ways that produce results favorable to them. Without special protections, they are left in a particularly weak position *vis-à-vis* the majority. When serious disagreements arise over the strategic direction or mismanagement of the corporation, capital lock-in reduces the power of an immobile, outvoted minority to place pressure on management to address concerns regarding business direction, efficiency, or profitability.<sup>31</sup> An even more serious possibility is that majority shareholders may use their management and/or shareholder rights to extract benefits for themselves at the expense of the corporation and minority shareholders.<sup>32</sup> The risk of minority shareholder exploitation is therefore inherent and characteristic of the close corporation.<sup>33</sup>

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28. Neville, *supra* note 25, at 258 (noting the potential for ordinary business disagreements to escalate into conflict).

29. *Id.*

30. See BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 33.

31. See *id.* at 35; Rock & Wachter, *supra* note 21, at 916 (noting that “the parties [are] locked into their investments to a much greater extent than in either the partnership or the publicly traded corporation”, and “minority shareholders are particularly vulnerable if there is a falling-out with the majority”); Neville, *supra* note 25, at 247–48 (pointing out that efficiency may not necessarily be a priority, leading to inefficient management and shareholder conflicts), 276–77 (lack of exit opportunities are especially acute in poorly-managed companies, and this undermines the minority shareholder’s ability to exert pressure on management and controlling shareholders to make improvements).

32. MARKUS KOEHNEN, OPPRESSION AND RELATED REMEDIES 448–49 (Thomson Carswell 2004); BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 9–10.

33. Means, *supra* note 26, at 1209.

### B. *Exit by Withdrawal as the Necessary Ultimate Solution*

The close corporation's two distinctive problems may be simply stated: conflicts between shareholders, and the need for minority shareholder protection. Shareholder conflicts may theoretically be resolved between the parties through dispute resolution mechanisms or temporary external intervention. External interventions include provisional directors that can vote to break deadlocks,<sup>34</sup> and alternative dispute resolution mechanisms such as mediation.<sup>35</sup> However, the efficacy of dispute resolution mechanisms or external interventions not involving exit of either party is limited to situations in which the conflict is not intractable, or where parties are committed to resolving the dispute.<sup>36</sup> Instead of resolving the conflict, temporary external interventions may even exacerbate matters if parties prove unable to reach a mutually agreeable compromise over a prolonged period of time, and would also be unacceptably intrusive if administered over the long term.<sup>37</sup> Similarly, judicial orders invalidating or restraining prejudicial acts do not by themselves put an end to shareholder conflict. As one national supreme court pertinently observed,

*[i]f the majority and minority cannot get along, litigation is not likely to improve matters between them. Anything short of a divorce is an invitation for repeat litigation in future. Thus, although the court may "direct or prohibit any act or cancel or vary any transaction or resolution" or "regulate the conduct of the affairs of the company in future", such orders are likely to provide only temporary relief.*<sup>38</sup>

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34. J.A.C. Hetherington & Michael P. Dooley, *Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 20–21 (1977).

35. MAXIMILIAN GOETTE, *DER EXIT DER MINDERHEIT AUS DER GMBH [EXIT OF THE MINORITY FROM THE GMBH]* 45–49 (Carl Heymanns 2014).

36. *Id.* at 45, 50–52; see Hetherington & Dooley, *supra* note 34, at 21 (“[The] remedy [of appointing a provisional director] ...is likely to work best where it is least needed, in resolving trivial disagreements.”).

37. See Hetherington & Dooley, *supra* note 34, at 21–25 (discussing some consequences of judicial remedies involving supervision of or other intervention into corporate affairs).

38. *Sembcorp Marine Ltd. v. PPL Holdings Pte Ltd.* [2013] SGCA 43, [2013] 4 SLR 193 ¶ 158 (Sing. Ct. App.) (emphasis in original) (quoting Wee Meng Seng, *Membership and Members' Rights*, in WALTER WOON ON COMPANY LAW ¶ 5.97 (Tan Cheng Han ed., rev. 3d ed., Sweet & Maxwell 2009)); see also PAUL L. DAVIES & SARAH WORTHINGTON, *GOWER'S PRINCIPLES OF MODERN COMPANY LAW* 680 ¶ 20-19 (10th ed., Sweet & Maxwell 2016) (“When business and, often, personal relations between quasi-partners have broken down and are incapable of reconstitution by a court, the only effective remedy is the minority's exit.”).

Ultimately, there must come a parting of the ways in cases of shareholder conflict not resolvable otherwise.<sup>39</sup> This is why exit solutions—such as withdrawal—fulfill a much-needed role.

For this Article, withdrawal is defined as “shareholder exit that occurs at the election of the shareholder desirous of exit and creates a monetary claim of the withdrawing shareholder for the value of their shares.” Note that shareholder “exit,” a term not infrequently encountered in close corporation literature,<sup>40</sup> is not synonymous with “withdrawal.” Here, “exit” is defined more broadly as “any legal mechanism by which a shareholder terminates their status as shareholder and the legal rights and obligations between the shareholder and the corporation and between the exiting shareholder and the other shareholders.” So defined, “exit” encompasses not just “withdrawal,” but also appraisal, dissolution, and even the voluntary transfer of shares by a shareholder to another person.<sup>41</sup> Comprising supplementary or baseline protection via statute, case law, doctrine, or some combination thereof,<sup>42</sup> withdrawal is to be distinguished from both *ex ante* self-help measures, such as buy-sell agreements, as well as self-help remedies predicated on majority power.<sup>43</sup>

With withdrawal offering minorities the possibility of leaving the corporation, minorities would not be subjected to majority power indefinitely.<sup>44</sup> Successful invocation of withdrawal achieves the basic objective of putting an end to the shareholder conflict by facilitating shareholder exit. A direct and potent response to majority opportunism and inter-shareholder conflict, withdrawal is the beleaguered minority’s last—and best—hope.

### C. *Withdrawal as a Common Feature in Leading Economies*

Perhaps the most compelling evidence for withdrawal remedies as an essential part of the solution to intractable shareholder conflict is that such remedies exist in developed corporate law jurisdictions.<sup>45</sup>

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39. See *supra* note 38 and accompanying text.

40. See e.g., BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 66–68; PAUL P. DE VRIES, EXIT RIGHTS OF MINORITY SHAREHOLDERS IN A PRIVATE LIMITED COMPANY (Kluwer 2010).

41. See *infra* Part III.B (discussing the availability of exit mechanisms—but not withdrawal—in Japan’s two historical leading close corporation forms).

42. It is a “widely acknowledged” notion that supplementary minority protection as a matter of general law in addition to any contractually-bargained protection is “indispensable.” Holger Fleischer, *Comparative Corporate Governance in Closely Held Corporations*, in OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 679, 707 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., Oxford University Press 2018).

43. E.g., formal squeeze-out techniques or expulsion. See generally O’NEAL AND THOMPSON’S OPPRESSION OF MINORITY SHAREHOLDERS, *supra* note 2, chs. 3–6 (discussing various techniques used to squeezeout minority shareholders).

44. GOETTE, *supra* note 35, at 21.

45. See generally Fleischer, *supra* note 42, at 701–03, 704.

Before delving into Japan's unique circumstances, it is worth taking a step back to consider other selected leading developed economies.

There is no single corporate law for the United States; each of the fifty states, the District of Columbia, and the inhabited territories (collectively "states") have their own corporation statutes and case law. Many states offer close corporation shareholders "oppression" remedies,<sup>46</sup> some of which provide for withdrawal by express statutory provision<sup>47</sup> and others through case law.<sup>48</sup> In the LLC, withdrawal remedies were historically available as of right across most of the United States,<sup>49</sup> and several states today continue to offer withdrawal as a default feature for members of LLCs.<sup>50</sup> Withdrawal's gradual retreat in LLC statutes appears to be driven by tax considerations<sup>51</sup> and has occurred without consideration of the implications of abolishing or curtailing withdrawal on the close corporation problem.<sup>52</sup>

The "unfair prejudice" remedy,<sup>53</sup> arguably the United Kingdom's most popular shareholder remedy, permits a plaintiff-shareholder to apply to court for relief on the grounds that the conduct of the company's affairs or an act (past or proposed) by or on behalf of the company is or would be "unfairly prejudicial"<sup>54</sup> to the plaintiff. The statute empowers the court with discretion to "make such order as it

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46. See generally O'NEAL AND THOMPSON's OPPRESSION OF MINORITY SHAREHOLDERS, *supra* note 2, § 7:11 (describing "oppression" remedies and giving examples from various states); see also *id.* § 7:12 (discussing remedies based on "reasonable expectations").

47. See, e.g., 805 ILL. COMP. STAT. 5/12.56(b)(11) (2017); LA. STAT. ANN. § 12:1-1435-1-1436 (2018); MICH. COMP. LAWS ANN. § 450.1489(1)(e) (West 2006); MINN. STAT. ANN. § 302A.751(2) (West 2011); N.D. CENT. CODE ANN. § 10-19.1-115(4) (West 2013); N.J. STAT. ANN. § 14A:12-7(8) (West 1988); OR. REV. STAT. § 60.952(2)(k), (5) (2015).

48. See, e.g., *G & N Aircraft, Inc. v. Boehm*, 743 N.E.2d 227, 244 (Ind. 2001).

49. Franklin A. Gevurtz, *Squeeze-Outs and Freeze-Outs in Limited Liability Companies*, 73 WASH. U. L.Q. 497, 514 n.95 (1995) (collecting and describing sources); see also Uniform Limited Liability Company Act §§ 601(1), 603(a)(1), 701 (NAT'L CONF. OF COMM'RS ON UNIF. STATE LAWS amended 1996) [hereinafter ULLCA 1996].

50. LA. STAT. ANN. §§ 12:1325(B), (C) (1995); MASS. GEN. LAWS ANN. ch. 156C, §§ 32, 36 (West 1995); MO. ANN. STAT. §§ 347.081, 347.103(2), 347.121(1) (West 1997).

51. See Douglas K. Moll, *Minority Oppression & The Limited Liability Company: Learning (Or Not) From Close Corporation History*, 40 WAKE FOREST L. REV. 883, 932-40 (2005) [hereinafter Moll, *Minority Oppression*] (discussing how changes in federal income taxation of LLCs allowing LLCs to freely elect taxation as a partnership or corporation removed the incentives of states to maintain withdrawal rights as a way of distinguishing LLCs from corporations; and how states, in attempting to make LLCs attractive business entities for estate and gift tax reasons, abolished withdrawal rights to reduce liquidity of LLC interests and thereby reduce the valuation of LLC interests for federal tax purposes).

52. See Douglas K. Moll, *Judicial Dissolution of the Limited Liability Company: A Statutory Analysis*, 19 TRANSACTIONS: TENN. J. BUS. L. 81, 106-07 (2017) [hereinafter Moll, *Judicial Dissolution*] (suggesting that states were unaware of or had overlooked the need to protect minority members from oppressive conduct in an earlier era when exit rights were common).

53. Companies Act 2006, c. 46, §§ 994-96 (U.K.).

54. *Id.* § 994(1).

thinks fit for giving relief in respect of the matters complained of<sup>55</sup> and specifies a nonexhaustive list of reliefs that the court may grant.<sup>56</sup> Court-ordered relief most commonly takes the form of a judicially-ordered buyout,<sup>57</sup> demonstrating the worth and centrality of withdrawal to the United Kingdom's shareholder remedies regime.<sup>58</sup>

Germany is arguably the earliest major jurisdiction to recognize a general withdrawal remedy (*Austritt aus wichtigem Grund*) for shareholders of the predominant *Gesellschaft mit beschränkter Haftung* (GmbH) closed corporation form despite the absence of express statutory provision.<sup>59</sup> Notwithstanding the GmbH's beginnings as a revolutionary invention of the German legislature, GmbH law has been little touched by major legislative reform but rather primarily shaped through German court decisions and academic literature. Member withdrawal ("*Austritt*") for "good cause" (*wichtiger Grund*) is an example of this *par excellence*. The flexible core concept of "*wichtiger Grund*," which supports withdrawal in a wide variety of circumstances, powerfully demonstrates withdrawal's value in the close corporation context.

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55. *Id.* § 996(1).

56. *Id.* § 996(2).

57. *Grace v. Biagioli* [2005] EWCA (Civ) 1222, [2006] 2 BCLC 70, [75] (Eng.) (Patten, J.) ("In most cases, the usual order to make will be the one requiring the respondents to buy out the petitioning shareholder at a price to be fixed by the court. This is normally the most appropriate order to deal with intra-company disputes involving small private companies."); ROBIN HOLLINGTON, *HOLLINGTON ON SHAREHOLDERS' RIGHTS* ¶ 8-44 (8th ed. Sweet & Maxwell 2017) ("The most important and commonly granted remedy, mentioned in s.996(2)(e), is an order for the purchase of the petitioner's shares either by another member or the company."); David Neuberger, *Company Law Reform: The Role of the Courts, in THE REFORM OF UNITED KINGDOM COMPANY LAW* 59, 69 (John de Lacey ed., Cavendish Publishing 2002).

58. *See generally* DAVIES & WORTHINGTON, *supra* note 38, ¶ 20-19 (linking the popularity of the unfair prejudice remedy to the buyout order (*i.e.*, withdrawal)).

59. The leading cases are Bundesgerichtshof [BGH] [Federal Court of Justice] Apr. 1, 1953, *ENTSCHEIDUNGEN DES BUNDESGERICHTSHOFES IN ZIVILSACHEN* [BGHZ] 9, 157 (Ger.) and Bundesgerichtshof [BGH] [Federal Court of Justice] Dec. 16, 1991, *ENTSCHEIDUNGEN DES BUNDESGERICHTSHOFES IN ZIVILSACHEN* [BGHZ] 116, 359 (Ger.). Most commentaries on the German GmbHG (Law on Limited Liability Companies) will have a chapter or section under the commentary to § 34 or as an appendix to § 34; *see also* GOETTE, *supra* note 35, at 97-143. For English sources, *see* DE VRIES, *supra* note 40, ch. 4; Tobias Brinkman, *Minority Protection under Section 459 of the Companies Act 1985: A Comparison with the Law of the German GmbH (Private Limited Company)*, 13 *EUR. BUS. L. REV.* 55, 78-79 (2002) (considering the withdrawal remedy [in the cited article, "right to resign"] in the context of valuation clauses in companies' articles of association, which companies use in attempts to provide alternative methods of share valuation for withdrawing shareholders, potentially to minority shareholders' disadvantage); Hugh T. Scogin, Jr., *Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem"*, 15 *MICH. J. INT'L L.* 127, 138-54 (1993) (detailing the development of the withdrawal remedy in Germany, dating back as far as 1930).

What about Japan, the second-largest economy for much of the postwar era, and which continues to be the second-largest developed economy in the world? The full story of withdrawal's place in Japan's close corporation law—spanning from the postwar era to the present—has yet to be told in English or Japanese. It unfolds over the next three Parts (III to V) in two acts. Part III presents a somewhat inconvenient historical truth: Japan's close corporations in the past did not have access to a withdrawal regime under Japanese corporate law. If withdrawal is crucial for close corporations, how did Japanese businesses thrive for decades despite its absence? Careful examination reveals that the Japanese developed workarounds and attempted—and failed—to create a withdrawal regime by law. The past ends and the present begins with the 2005 *Kaisha-hō*, when a new close corporation was introduced, which included a withdrawal regime.<sup>60</sup> Critical analysis of this new entity and withdrawal regime are respectively the subjects of Parts IV and V.

### III. THE PAST: THE CONTEXT AND PUZZLE OF JAPAN'S CLOSE CORPORATION LAW

If there is a single event in the postwar era marking when Japanese corporate law of the “past” ended and “contemporary” Japanese corporate law began, it would be the enactment of the *Kaisha-hō* in 2005.<sup>61</sup> In this Part, the hitherto untold story of Japan's close corporation law and withdrawal before 2005 unfolds to reveal—and resolve—a historical mystery: How did the world's second-largest economy get by without offering a withdrawal regime for its close corporations?

#### A. Japan's Two Close Corporation Forms: Kabushiki Kaisha (“KK”) and Yūgen Kaisha (“YK”)

Before 2005, the two corporate forms used most often for close corporations were the KK<sup>62</sup> (“Stock Corporation”<sup>63</sup>) and the YK

60. See *infra* Part IV.

61. See generally *Kaisha-hō* [Companies Act], Law No. 86 of 2005 (Japan).

62. Due to a Japanese morphophonological phenomenon known as *rendaku* (連濁), when preceded by a modifier such as 株式, 有限, 持分, 合名, 合資, 合同, 合弁, etc., the word 会社 is usually pronounced *gaisha* (not *kaisha*) in speech. However, for clarity, *rendaku* will be largely disregarded in this Article.

63. I use the word “corporation” deliberately to distinguish the KK from the *mochibun kaisha* (“membership company”). Cf. *infra* note 169. In so doing I depart from “stock company”, which is the preferred translation of the latest edition of the semi-official dictionary adopted by the Japanese Government. JAPANESE LAW TRANSLATION COUNCIL, STANDARD LEGAL TERMS DICTIONARY 54 (ver. 11.0, Mar. 2019), JAPANESE LAW TRANSLATION COUNCIL, available at <http://www.japaneselawtranslation.go.jp/dict/download?re=2> (last visited Feb. 23, 2020).

(“Limited Liability Corporation”). A creature of Japan’s venerable *Shō-hō* (Commercial Code),<sup>64</sup> the KK came to be widely used by small, even *de facto* single-owner businesses in the postwar era.<sup>65</sup> Although share transfer restrictions were legally prohibited in KKs for some years, this prohibition posed no practical obstacle to the KK’s adoption as a close corporation form; even before their legalization in 1966, a significant proportion of small KKs had some form of share transfer restrictions.<sup>66</sup> Terminologically, equity interests in KKs are “shares” (*kabu*)<sup>67</sup> and holders of these interests are “shareholders” (*kabunushi*).<sup>68</sup>

The YK, Japan’s second close corporation form before 2005, was introduced in 1938 by the *Yūgen Kaisha-hō* (“Limited Liability Corporations Act”) (YK Act).<sup>69</sup> In contrast with the KK, YK equity interests are technically *mochibun*<sup>70</sup> (which will be translated as “membership interests” for the purposes of this Article<sup>71</sup>), and holders of these interests are referred to as “members” (*sha’in*).<sup>72</sup> The YK was modeled primarily on the German GmbH due to the GmbH’s success and influence and because Japan’s commercial law was based on Germany’s; however, other foreign influences were also taken into account.<sup>73</sup> Despite both its greater suitability for small businesses as a matter of design<sup>74</sup> and its strong growth over the decades,<sup>75</sup> the YK

64. *Shō-hō* [Commercial Code], Law No. 48 of 1899. The *Shō-hō* itself is still partly in force, but provisions applicable to KKs and other corporate entities (*gōmei kaisha* and *gōshi kaisha*) have been repealed and replaced by the *Kaisha-hō*. Unless otherwise specified, all references to *Shō-hō* provisions are as of the date of repeal.

65. Takahashi Eiji, *Nihon ni okeru Heisa-teki Shihon Kaisha no Hatten to Hō* [*The Development and the Law of Closed-type Companies of Capital*], 1914 SHŌJI HŌMU 4, 5 (2010) [hereinafter Takahashi, *Closed-type Companies*].

66. *Id.*

67. The semi-official dictionary adopted by the Japanese Government also notes that it is permissible to translate *kabu* as “stock” “depending on context”. *Kabu*, JAPANESE LAW TRANSLATION COUNCIL, STANDARD LEGAL TERMS DICTIONARY 53 (Mar. 2019 ed.). However, given that “shares” tends to be the more commonly used variant in English-language writing on Japanese corporate law, this Article will use “shares” while acknowledging the linguistic tension between “stock corporation” and “shares”.

68. In similar vein, “stockholder” is also permissible “depending on context.” *Id.* at 54.

69. *Yūgen Kaisha-hō* [Limited Liability Corporations Act], Law No. 74 of 1938, repealed by Law No. 87 of 2005 (Japan) [hereinafter YK Act].

70. *Id.* at arts. 18–19 (repealed).

71. This is for the purpose of distinguishing the YK from the KK.

72. YK Act arts. 18–19ff.

73. SAKAMAKI TOSHIO, HEISA-TEKI KAISHA NO HŌRI TO RIPPŌ [CLOSE CORPORATIONS: DOCTRINE AND LEGISLATION] 238–39 (Nipponhyōronsha 1973) (explaining why the legislature also took into consideration the laws of England, France, and Austria).

74. SUZUKI TAKEO, SHIN-PAN KAISHA HŌ [CORPORATE LAW: NEW EDITION] 361, 363 n.1 (5th rev. ed., Kōbundō 1994).

75. See TAKAHASHI EIJI, JŪZOKU KAISHA NI OKERU SHŌSŪ KABU’NUSHI NO HOGO [PROTECTION OF MINORITY SHAREHOLDERS IN DEPENDENT SUBSIDIARIES] 215 (Yūhikaku



did not achieve dominance over the KK during its lifetime for reasons including the YK Act's poor drafting and structure<sup>76</sup> and the YK's negative signaling among business people.<sup>77</sup>

Together with other reasons,<sup>78</sup> these problems led to the repeal of the YK Act<sup>79</sup> in conjunction with the enactment of the *Kaisha-hō*. Since then, no new YKs can be incorporated; all YKs existing as of the *Kaisha-hō*'s entry into force are formally and involuntarily converted into KKs with special transitional governing provisions.<sup>80</sup> Accordingly, YKs today are technically "stock corporations" with "shares." A significant number of ex-YKs still remain and, as of 2017, number about 1.57 million.<sup>81</sup>

1998); Harald Baum & Gen Goto, *Die japanische LLP im gesellschaftsrechtlichen Kontext* [*The J-LLP in the Corporate Law Context*], 41 J. JAPANESE L. 89, 97 tbl.1 (2016) (providing data); Michiyo Hamada, *Forthcoming Legislative Reform of Japanese Corporation Law: Comparative Study of Japanese and American Close Corporation Law* 4 fig.2 (1986) (unpublished research paper, Harvard Law School) [hereinafter Hamada, *Forthcoming Legislative Reform*].

76. See SAKAMAKI, *supra* note 73, at 240 (describing the YK Act's heavy use of cross-references to the Commercial Code).

77. See Kitazawa Masahiro & Hamada Michiyo, *Shō-Kibo Kabushiki Kaisha oyobi Yūgen Kaisha ni kansuru Jittai, Iken Chōsa: Chūkan Hōkoku* [*Surveys on the Realities and Opinions Concerning Small-Scale KKs and YKs: Interim Report*], 962 SHŌJI HŌMU 21, 30 tbl.13, 31 tbl.14 (1983); Takahashi, *Closed-type Companies*, *supra* note 65, at 5.

78. See Aizawa Tetsu & Kōriya Daisuke, *Kaisha Hōsei no Gendaika ni Tomonau Jisshitsu Kaisei ni Gaiyō to Kihon-teki na Kangaekata* [*The Outline and Fundamental Philosophy of the Substantive Reforms in Connection with the Modernization of the Corporate Law System*], in RITSUAN TANTŌSHA NI YORU SHIN-KAISHA HŌ NO KAISETSU [THE DRAFTSMEN'S COMMENTARY ON THE NEW COMPANIES ACT] 1, 9 (Aizawa Tetsu ed., Bessatsu Shōji Hōmu No. 295, Shōjihōmu 2006) (stating that the merger of the KK and the YK was a response to, among other things, the erosion of the conceptual distinction between the two forms in business practice, and the discordance between how the two forms regulate various aspects [such as the number and term limits of directors and whether features such as a board of directors (*torishimariyaku-kai*) or one or more statutory auditors (*kansayaku*) are mandatory]).

79. Takahashi, *Closed-type Companies*, *supra* note 65, at 6.

80. Technically, the conversion of YKs into KKs is not provided for in the *Kaisha-hō* itself, but a companion act that, among other things, also repealed the YK Act and other companies legislation that accumulated over the decades. The conversion is made pursuant to *Kaisha Hō no Shikō ni tomonau Kanren Hōritsu no Seibi-tō ni kansuru Hōritsu* [Act on Arrangement of Relevant Acts Incidental to Enforcement of the Companies Act], Law No. 87 of 2005, art. 2 (Japan) [hereinafter *Seibi-hō*]; see also Yamamoto Norimitsu, *Yūgen Kaisha Hō no Haishi ni tomonau Keika Sochi* [*Transitional Arrangements Accompanying the Repeal of the YK Act*], in RITSUAN TANTŌSHA NI YORU SHIN-KAISHA HŌ NO KAISETSU [THE DRAFTSMEN'S COMMENTARY ON THE NEW COMPANIES ACT] 229, 230–38 (Aizawa Tetsu ed., Bessatsu Shōji Hōmu No. 295, Shōjihōmu 2006) (describing the changes); Eiji Takahashi & Madoka Shimizu, *The Future of Japanese Corporate Governance: The 2005 Reform*, 19 J. JAPANESE L. 35, 41, 45–46 (2005) (discussing changes to the KK).

81. Compare KANDA HIDEKI, *KAISHA-HŌ* [CORPORATE LAW] 7 n.1 (20th ed. Yūhikaku 2018) (1.573 million as of October 2017) with Baum & Goto, *supra* note 75, at 97 tbl.1 (1.64 million as of 2014).

For ease of exposition and unless the context otherwise specifies that only the KK is discussed, in the rest of this Article, “shareholder(s)” is used more broadly to refer to both KK shareholders and YK members (especially in Part II) as well as holders of equity interests in corporation forms more generally (particularly Parts II and VI).

B. *Exit Without Withdrawal: The Exceptionalism of Japanese Close Corporation Law*

The central claim advanced here in Part III is that withdrawal is completely absent from Japan’s two widely adopted<sup>82</sup> close corporation forms. As this renders the world’s erstwhile second-largest economy an outlier among other comparable leading economies, it deserves scrutiny. This subpart demonstrates how, despite the existence of various exit mechanisms seemingly applicable to Japanese close corporations before 2005, *withdrawal* specifically was not available.

To appreciate Japanese corporate law’s exceptionalism, grasping the distinction between *withdrawal* and *exit* is critical. As defined above at Part II.B, withdrawal is “shareholder exit that occurs at the election of the shareholder desirous of exit and creates a monetary claim of the withdrawing shareholder for the value of their shares.”<sup>83</sup> This Article is *not* making the claim that the KK and YK lacked any form of *exit*. In fact, both close corporation forms offered, and the KK continues to offer, under the *Kaisha-hō*, a variety of exit mechanisms such as judicial dissolution,<sup>84</sup> appraisal (KK only),<sup>85</sup> as well as the right to transfer equity to another person. This last exit mechanism of voluntary transfer of KK shares/YK membership interests to another person<sup>86</sup>—presumably in exchange for money or equivalent benefits—is fundamental to Japanese corporate law. In the context of KKs with share transfer restrictions (and historically, for YKs as well), however, this is further subject to a relatively complex system of rules. Although

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82. See *infra* note 148 and accompanying text (discussing the relative popularity of YKs and KKs compared to other business entities in Japan).

83. See *supra* Part II.B, at 16.

84. See *Shō-hō*, [Commercial Code], Law No. 48 of 1899, art. 406-2 (Japan) (repealed) (providing for a shareholders’ right to apply to a court for dissolution of a company); YK Act, art. 71-2 (repealed) (same); *Kaisha-hō*, [Companies Act], Law No. 86 of 2005, art. 833(1) (Japan) (same).

85. See generally Moritz Bälz, *Appraisal Rights in Japanese Corporate Law*, 13 J. JAPANESE L. 152 (2002); Alan K. Koh, *Appraising Japan’s Appraisal Remedy*, 62 AM. J. COMP. L. 417 (2014).

86. *Shō-hō*, art. 204(1) (repealed); YK Act, art. 19(1) (repealed) (providing for transfer to other members of the YK); *Kaisha-hō*, art. 127.

not well known in the English-language literature,<sup>87</sup> these rules are, with minor modifications, still good law for KKs under the *Kaisha-hō*<sup>88</sup> (including ex-YKs<sup>89</sup>). The analysis to follow will show how this restricted-transfer equity regime—which has few parallels in the corporate laws of other leading economies<sup>90</sup>—is not a “withdrawal” mechanism within the meaning of this Article.<sup>91</sup>

As a matter of corporate law,<sup>92</sup> transfer of shares (as well as the rights and status of a shareholder) as a means of shareholder exit is legally straightforward when the corporation is a KK with no share transfer restrictions. However, in KKs that wish to preserve their “close” character using a legal mechanism,<sup>93</sup> shares may be subject to transfer restrictions (“restricted-transfer shares” *jōto-seigen kabushiki*) via provision in the corporation’s constitution (*teikan*).<sup>94</sup> Although a transfer of shares is binding as between transferor and transferee without the need for approval by an external party,<sup>95</sup> in the

87. For an alternative description of this regime under the *Kaisha-hō*, see, e.g., ICHIRO KAWAMOTO, YASUHIRO KAWAGUCHI & TAKAYUKI KIHIRA, CORPORATIONS AND PARTNERSHIPS IN JAPAN 153–55 (Wolters Kluwer 2012); HIROSHI ODA, JAPANESE LAW 239 (3d ed., Oxford University Press 2009).

88. *Kaisha-hō*, arts. 136–45 (establishing rules governing when and how a shareholder may transfer their shares).

89. *Seibi-hō*, art. 9.

90. The sole exception that the author knows of is the Republic of Korea. *See* Sangbeop [Commercial Act], Act No. 1000, Jan. 20, 1962, *amended by* Act No. 15755, Sept. 18, 2018, arts. 335 to 335-7 (S. Kor.), *translated in* Korea Legislation Research Institute online database, [https://elaw.klri.re.kr/eng\\_service/lawView.do?lang=ENG&hseq=51179](https://elaw.klri.re.kr/eng_service/lawView.do?lang=ENG&hseq=51179) (last visited Aug. 19, 2020) [<https://perma.cc/BJW7-8EU4>] (archived Aug. 19, 2020). Due to its potentially sensitive nature, as an outsider, the author shall not comment on the connection, if any, between these two corporate law regimes.

91. The discussion of restricted-transfer shares in this Subpart is the author’s response to feedback from Professor Goto Gen and Professor Shishido Zen’ichi on earlier versions of this Article.

92. In line with this Article’s focus on close corporations, the Article does not discuss the securities law aspects.

93. EGASHIRA KENJIRŌ, *KABUSHIKI KAISHA HŌ* [THE LAWS OF STOCK CORPORATIONS] 233 (7th ed., Yūhikaku 2017) [hereinafter EGASHIRA 2017] (observing that there is a strong demand in closed-type (*heisa-gata*) corporations to keep the shareholder body limited to persons who are in a relationship of interpersonal trust). Interestingly, when restricted-transfer shares were re-introduced by law reform in 1966, one of the motivations may have been to prevent takeovers of KKs by foreign capital. *Id.* at 234 n.3.

94. *Shō-hō*, [Commercial Code], Law No. 48 of 1899, art. 204(1) proviso (Japan) (repealed); *Kaisha-hō*, [Companies Act], Law No. 86 of 2005, art. 2(xvii) (Japan) (defining *jōto seigen kabushiki*); *id.* at arts. 107(2)(i), 108(2)(iv) (requiring that a transfer restriction must be specified in the constitution).

95. Imai Hiroshi, § 204 / 2 [§ 204-2], in III SHIN-PAN CHŪSHAKU KAISHA HŌ: KABUSHIKI (1) [CORPORATE LAW COMMENTARY, NEW EDITION: SHARES (1)] 79, 83–84 (Ueyanagi Katsurō, Ōtori Tsuneo & Takeuchi Akio eds., Yūhikaku 1986) (noting that a transfer of shares pursuant to a contract for the sale and purchase of shares is effective as between the parties); KANDA, *supra* note 81, at 112 (stating that a transfer is effective between the parties with “manifestation of intention” (*ishi hyōji*)).

case of restricted-transfer shares a transfer does not bind the KK or other third parties unless such transfer is approved by the corporation.<sup>96</sup> Both the transferor and the transferee have the right to request the KK to approve the transfer.<sup>97</sup> Approval may either be expressly granted by resolution of the proper organ of the KK,<sup>98</sup> or deemed to have been implicitly given if approval is not communicated by the proper organ within a specified timeframe.<sup>99</sup> For YKs, transfer of membership interest from one existing YK member to another YK member required no further approval to be binding on the YK.<sup>100</sup> Transfer to a third party (i.e., to a non-YK member), however, was subject to similar rules as those for KK restricted-transfer shares.<sup>101</sup>

What happens if the corporation refuses to grant approval? The distinctive feature of Japan's legal framework for KK restricted-transfer shares and YK membership interests is how it accommodated under the *Shō-hō*, and continues to accommodate for KKs under the *Kaisha-hō*, two competing aims: maintaining the "close" aspect of a close corporation and protecting the interest of a shareholder or member in recovering their investment.<sup>102</sup> The corporation has the power to refuse approval of the transfer,<sup>103</sup> but the transferor and transferee have alternative recourse in the right to demand that the corporation designate (*shitei-su / shitei-suru*) an alternative purchaser for the shares ("designated purchaser" *sono kabushiki* [YK: *mochibun*] *wo kaiuku beki mono / shitei kaitori-nin*), which may be the corporation

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96. *Kaisha-hō*, arts. 130(1), 133(1), 134(i), (ii); Imai, *supra* note 95, at 83.

97. *Shō-hō*, arts. 204-2(1) (transferor), 204-5(1) (transferee) (all repealed); *Kaisha-hō*, arts. 136, 137(1) (applying to transferors and transferees, respectively).

98. *Kaisha-hō*, art. 139(1) (depending on the specific subtype of KK, a resolution of either the shareholder meeting [*kabunushi sōkai*] or board of directors [*torishimariyaku-kai*]); Ueyanagi Katsurō, § 204, in III SHIN-PAN CHŪSHAKU KAISHA HŌ: KABUSHIKI (1) [CORPORATE LAW COMMENTARY, NEW EDITION: SHARES (1)] 53, 64–65 (Ueyanagi Katsurō, Ōtori Tsuneko & Takeuchi Akio eds., Yūhikaku 1986) (stating that, in the context of the *Shō-hō* era, according to majority scholarly opinion, only the board may be vested with the power to approve a transfer).

99. Approval is deemed to be given if the proper organ fails to communicate refusal within a specified time period. *Shō-hō*, art. 204-2(7) (repealed); *Kaisha-hō*, art. 145.

100. YK Act, art. 19(1) (repealed).

101. *Id.* art. 19(2) (transfer to non-members required approval of the members' meeting); *id.* 19(3) (transferor had right to request approval of transfer); *id.* 19(7) (transferee had right to request approval of transfer); *id.* 19(3)–(7) (applying various *Shō-hō* provisions on restricted-transfer shares *mutatis mutandis*) (all repealed).

102. See Ueyanagi, *supra* note 98, at 58–59, 60, 66 (describing the legislative policy behind the 1966 reform introducing the restricted-transfer share regime).

103. Albeit not an unfettered power. See, e.g., EGASHIRA KENJIRŌ, KABUSHIKI KAISHA HŌ, YŪGEN KAISHA HŌ [LAWS OF STOCK CORPORATIONS AND LIMITED LIABILITY COMPANIES] 214 n.7 (4th ed. Yūhikaku 2005) [hereinafter EGASHIRA 2005] (summarizing constraints).

itself.<sup>104</sup> Under the *Shō-hō* and *YK Act*, the designated purchaser also had the right to demand that the original shareholder (transferor) transfer to the designated purchaser the shares/membership interest at issue.<sup>105</sup> Under the *Kaisha-hō*, the corporation or other designated purchaser is required to give a statutorily prescribed notice to the transferor—an act that also creates a sale and purchase contract for the shares binding on the transferor and the designated purchaser.<sup>106</sup> The purchase price for the shares is, in principle, up to the parties (the transferor and the designated purchaser) to negotiate between themselves.<sup>107</sup> However, either party may within twenty days of the date of the demand to transfer (*Shō-hō*) or the date of the statutorily prescribed notice (*Kaisha-hō*) apply to court for a judicial determination of the purchase price.<sup>108</sup>

The regime governing KK restricted-transfer shares and YK membership interests described above offers close corporation shareholders a form of “exit,” but not “withdrawal.” Properly understood, the KK/YK transfer restriction system is premised on the existence of a willing purchaser for the shares in the first place; if there is no prospective transferee to begin with, the rules did not (and, under current KK law, do not) provide an exit mechanism. All the rules do is to create a statutory right of a shareholder/member to force the corporation to make a choice between approving a private transaction and purchasing (or arranging someone else to purchase) the shares, and provide them with a mechanism for disputes over valuation of (but not liability to purchase) the shares. The system does not assist a shareholder who is for any reason—including illegal, oppressive, or otherwise unfair acts of other participants in the corporation, or any other circumstances of the corporation—unable to find a person willing to purchase their shares at an acceptable price. In other words, the KK/YK system is not a solution to the close corporation problem.

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104. *Shō-hō*, arts. 204-2(1) (transferor), 204-5(1) (transferee), 204-3-2(1) (the KK's board may designate the KK itself as the purchaser) (all repealed); *YK Act*, arts. 19(3) (transferor), 19(7) (transferee), 19(6) (members' meeting may designate the YK as the purchaser) (all repealed); *Kaisha-hō*, arts. 136 (transferor), 137(1) (transferee), 140(1) (as a starting point, the KK itself should (and may) purchase the shares), 140(4) (the KK may, as an alternative, specify another person as the designated purchaser). When the corporation is the designated purchaser (effectively creating a share buyback scenario), difficult issues of capital maintenance arise (*Kaisha-hō*); in the interests of brevity, the Article does not discuss them here.

105. *Shō-hō*, arts. 204-3(1), 204-5(1) (applying articles 204-3, 204-3-2, and 204-4 *mutatis mutandis*) (all repealed); *YK Act*, art. 19(5) (applying article 204-3(1) of the *Shō-hō mutatis mutandis*) (repealed).

106. See *Kaisha-hō*, arts. 141, 142 (requiring the purchaser in a stock transfer to give notice of purchase); EGASHIRA 2017, *supra* note 93, at 242.

107. See *Shō-hō*, art. 204-4(1) (repealed); *YK Act*, art. 19(5) (applying article 204-4 of the *Shō-hō mutatis mutandis*) (repealed); *Kaisha-hō*, art. 144(1), (7) (applying article 144(1) *mutatis mutandis*); EGASHIRA 2005, *supra* note 103, at 216.

108. *Shō-hō*, art. 204-4(3) (repealed); *YK Act*, art. 19(5) (repealed); *Kaisha-hō*, arts. 144(2), (7) (applying article 144(2) *mutatis mutandis*).

Conversely, withdrawal does not require a willing purchaser to exist; the very essence of withdrawal is the creation of a monetary claim by the shareholder against some person, who may (although not necessarily) be made liable to pay the withdrawing shareholder by force of corporate law rather than via consent. In requiring neither a market for shares nor the mercy of the (potentially oppressive) majority, withdrawal is a solution to the close corporation problem that a minority shareholder may resort to without depending on any actor but corporate law and the legal system. Accordingly, the KK/YK transfer restriction system is not withdrawal in any form. Rather, it is, at best, analogizable to a statutory right of first refusal to the corporation (or a person as designated by the corporation) with a court-administered valuation mechanism.

D. *The Puzzle: Does Withdrawal's Historical Absence from Japan's Close Corporations Undermine the Case for Withdrawal?*

By all appearances, pre-*Kaisha-hō* Japanese corporate law seems to be the outlier among leading nations on legal withdrawal for close corporations. For better or for worse, the Japanese generally do not make adequate *ex ante* contractual arrangements with a view to forestalling or resolving possible future close corporation disputes.<sup>109</sup> Yet, despite withdrawal's absence in both the KK and the YK, whether in corporate law or widely adopted contractual practice, Japan has become one of the world's leading economies.<sup>110</sup> A puzzle thus presents itself: is Japan the glaring exception proving that withdrawal remedies are *not* essential to close corporation law in general (i.e., contrary to what Part II.B<sup>111</sup> has advanced above)?

To solve this puzzle, Part III.C makes three points. First, it shows that there was popular demand for withdrawal; unmet by the deficient formal legal regime, this demand was addressed by creative, functional substitutes, albeit only partly and imperfectly. Second, it also provides

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109. Ueyanagi Katsurō et al., *SHIMPOJIUMU: Shōkibo, Heisa Kaisha no Rippō* [Symposium: Legislating for Small- and Closed Corporations], 46 SHIHŌ 117, 140 (1984) (Statement by Hamada Michiyo). However, share transfer restrictions were adopted almost universally (>90%) in Kks incorporated since 1975. Kitazawa & Hamada, *supra* note 77, at 30 tbl.12. Express share transfer restrictions were unnecessary in the YK; any transfer of membership interests to persons other than existing YK members required approval of the members in general meeting. YK Act, art. 19(2) (repealed). Transfers between members did not require approval. *Id.* art. 19(1) (repealed).

110. As of 2019, Japan was the third largest economy in the world by gross domestic product after only the US and the People's Republic of China. *Gross domestic product 2019*, WORLD BANK (July 1, 2020), <https://databank.worldbank.org/data/download/GDP.pdf> [https://perma.cc/9T4T-GG9V] (archived Aug. 19, 2020).

111. *See supra* Part II.B (emphasizing the necessity of withdrawal remedies).

a concise account of a serious, though abortive, attempt to introduce a formal withdrawal regime through law reform that nonetheless revealed a scholarly consensus over the necessity of withdrawal as a legal regime. Finally, it explains why Japanese businesses—despite the deficiency of KKs and YKs with respect to legal withdrawal solutions—nonetheless adopted these forms in droves for other business reasons. These three points, which arose out of Japan’s unique circumstances, demonstrate withdrawal’s practical relevance, despite its absence from Japan’s corporate law.

### 1. Partial, Functional Substitutes for a Formal Withdrawal Regime

Without any specific statutory provision entitling them to relief by withdrawal, aggrieved shareholders—and their lawyers—had to get creative. Shareholders would resort to threatening the company and its controlling shareholders with disclosure of illegal activities, such as tax evasion.<sup>112</sup> While presumably effective, this nonetheless amounts to borderline or actual extortion. Attorneys representing aggrieved minority shareholders often adopted the more legalistic approach of lawsuits challenging corporate procedures for noncompliance with necessary legal formalities.<sup>113</sup> Examples include seeking invalidation of a shareholder resolution or a declaration of the nonexistence thereof<sup>114</sup> or a declaration of nullity of a board resolution.<sup>115</sup> Other techniques involve combinations of legal mechanisms. For example, a challenge to the validity of a shareholder resolution appointing a

112. Hamada Michiyo, *Kabunushi no Mujōken Kabushiki Kaitori Seikyū-ken (ichi)* [*The Shareholder’s Right to Demand a Share Buyout at Will (Part 1)*], 982 SHŌJI HŌMU 59, 63 (1983) [hereinafter Hamada, *Shareholder’s Right*].

113. See generally Harald Baum & Eiji Takahashi, *Klagen gegen fehlerhafte Hauptversammlungsbeschlüsse im japanischen Aktienrecht* [*Legal Challenges against Flawed Shareholder Meeting Resolutions in Japanese KK Law*], 32 J. JAPANESE L. 153 (2011). European jurisdictions also offer similar avenues for shareholder challenges, although not the UK. BACHMANN, EIDENMÜLLER, ENGERT, FLEISCHER & SCHÖN, *supra* note 19, at 63–64.

114. Shō-hō, [Commercial Code], Law No. 48 of 1899, arts. 247(1)(i), 252 (Japan) (repealed) (applying to the KK); YK Act, art 41 (repealed) (applying to the YK); Kaisha-hō, [Companies Act], Law No. 86 of 2005 arts. 830–31 (Japan) (applying to the KK). No statutory equivalent exists for the GK because there is no mandatory requirement that the members, each and every one of whom have executive powers by default (Kaisha-hō, art. 590(1)), to pass formal “resolutions” (*ketsugi*) at a “meeting” (*sōkai*). By default, decisions on day-to-day business (*jōmu*) may be taken by members individually unless objected to by another member (Kaisha-hō, art 590(3)), and by simple majority in the case of ordinary business decisions with member objections and management decisions (*gyōmu*) (Kaisha-hō, art. 590(2)). See generally Shishido Zen’ichi, *Dai-590-jō* [*Article 590*], in 14 KAISHA HŌ KONMENTĀRU: MOCHIBUN KAISHA (1) [COMMENTARY ON THE COMPANIES ACT: MEMBERSHIP COMPANIES (1)] 133, 134–35 (Kanda Hideki ed., Shōjihōmu 2014); see also EGASHIRA 2017, *supra* note 93, at 366 n.1.

115. See Saikō Saibansho [Sup. Ct.] Nov. 8, 1972, 26(9) Minshū 1489; EGASHIRA 2005, *supra* note 103, at 359, 360 n.16; EGASHIRA 2017, *supra* note 93, at 425.

director<sup>116</sup> (or an application to remove a director for cause<sup>117</sup>) could be combined with an application for provisional court orders (*kari-shobun*; similar to interim injunctions) that would suspend the director in question and appoint in their place an acting director.<sup>118</sup>

These lawsuits in and of themselves did nothing to resolve the underlying issues in dispute,<sup>119</sup> even if the aggrieved shareholder won the lawsuit itself.<sup>120</sup> If the aggrieved shareholder's complaint was, on its face, that a shareholder resolution was not passed at a properly convened shareholder meeting, all the controlling majority shareholders needed to do was to convene a meeting properly and pass the resolution correctly next time. Why, then, did attorneys commence such lawsuits when their clients hardly cared about corporate law formalities?<sup>121</sup> Because these lawsuits worked, if indirectly. First, given that noncompliance with corporate formalities in small, closely held corporations was an endemic problem,<sup>122</sup> it was easy to find some basis to commence such lawsuits, and even win.<sup>123</sup> Second, neither the

116. See *infra* note 118 and accompanying text (discussing the mechanisms of challenges to resolutions).

117. Shōhō, arts. 257(3), 257-3(4) (repealed) (KK); YK Act, art. 31-3 (repealed); Kaisha-hō, arts. 854, 860 (applying to the removal of directors and other KK officers and termination of executive members' rights to manage or represent the company in GKs and other membership companies, respectively).

118. Hamada, *Shareholder's Right*, *supra* note 112, at 63 (citing Commercial Code articles 270 and 271 as the basis). Article 270 was subsequently repealed in 1990; the current equivalent is Minji Hozen-hō [Civil Provisional Remedies Act], Law No. 91 of 1989, art. 23(2) (Japan). Article 271 was also repealed; today's equivalents are Kaisha-hō, arts. 352 (pertaining to KKs), 603 (applying to membership companies including GKs) read with Minji Hozen-hō, art. 56.

119. See Shishido Zen'ichi, *Heisa Kaisha ni Okeru Naibu Funsō no Kaiketsu to Keizai-teki Kōsei* [Ways to Achieve Financial Fairness in Coping with Internal Dissension in the Closely-Held Corporation], 46 SHIHŌ 237, 237 (1984) [hereinafter Shishido, *Ways to Achieve*].

120. See Shishido Zen'ichi, *Problems of the Closely Held Corporation: A Comparative Study of the Japanese and American Legal Systems and a Critique of the Japanese Tentative Draft on Close Corporations*, 38 AM. J. COMP. L. 337, 341-44 (1990) [hereinafter Shishido, *Problems*] (explaining how the Japanese legal process does not directly assist even a successful shareholder plaintiff in achieving their desired outcome); Hamada, *Shareholder's Right*, *supra* note 112, at 63.

121. Hamada, *Shareholder's Right*, *supra* note 112, at 63. (observing that minority shareholders had little awareness that non-compliance with corporate formalities is unlawful, and that clients were often surprised when their attorneys suggested bringing procedural challenges as a means of resolving shareholder disputes).

122. *Id.*; see also AOTAKE SHŌICHI, SHŌ-KIBO HEISA KAISHA NO HŌKISEI [LEGAL REGULATION OF SMALL-SCALE CLOSED CORPORATIONS], 318-19 (Bunshindō 1979) (observing that many small-scale KKs have neither the inclination nor ability to comply with the law governing KKs); Ueyanagi et al., *supra* note 109, at 119 (Statement by Imanaka Toshiaki) (a legal practitioner observing that Japan lacked a spirit of legal compliance); Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 15.

123. Shishido Zen'ichi, *Heisa Kaisha ni okeru Naibu Funsō no Kaiketsu to Keizai-teki Kōsei (ichi)* [Ways to Achieve Financial Fairness in Coping with Internal Dissensions



attorneys nor the shareholders needed or even necessarily wanted to succeed in these lawsuits *per se*.<sup>124</sup> Instead, it was the shock—especially to a small company—caused by the commencement of legal proceedings that brought the relevant parties to the negotiating table.<sup>125</sup> Ultimately, the dispute would almost invariably be resolved with the *factual* withdrawal of one of the parties in conflict via settlement that is facilitated, with great effort, by the parties' attorneys and even the judges hearing the lawsuits.<sup>126</sup>

That this phenomenon went largely unnoticed by foreign observers is unsurprising.<sup>127</sup> Without adequate knowledge of Japan's somewhat peculiar context, even careful analysis of the reported cases on actions challenging corporate procedures would have yielded little insight. Constrained by doctrine as to the scope of the facts and issues that could be addressed, in cases where only peripheral issues could be litigated, Japanese court judgments could have said little to shed light on the real, underlying core issues.<sup>128</sup> Within Japan's legal community, however, the practice of using lawsuits over corporate legal formalities for the purpose of resolving shareholder disputes as described above appeared to be established and well known. Not only were astute academic commentators such as Hamada Michiyo<sup>129</sup> familiar with it, even the Ministry of Justice's law reform officers expressly acknowledged the practice's existence.<sup>130</sup>

Even though the practical workarounds arguably achieved a measure of success by prompting settlement with *factual* withdrawal as the result in many cases, they were not without their shortcomings. For example, cooperation from understanding judges was key. Yet not all judges were sufficiently aware, as a string of Japanese judgments featured dismissals, on grounds of abuse, of shareholder applications

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*in the Closely Held Corporation (Part 1)*], 101 HŌGAKU KYŌKAI ZASSHI 505, 541 (1984) (reporting that shareholder plaintiffs won in a majority of over 100 reported decisions from 1950 to 1982 on shareholder challenges to shareholder resolutions).

124. See *supra* note 121 and accompanying text.

125. See Hamada, *Shareholder's Right*, *supra* note 112, at 63.

126. See *id.* at 63–64; Ueyanagi et al, *supra* note 109, at 129, 141 (Statement by Hamada Michiyo).

127. The sole published English-language source discussing this appears to be Shishido, *Problems*, *supra* note 120, at 342–44 (describing how such lawsuits operate within Japan's civil litigation context). Hamada's 1986 Harvard Law School paper (Hamada, *supra* note 75) is, while insightful and powerfully written, unfortunately unpublished.

128. Shishido, *Ways to Achieve*, *supra* note 119, at 237–38; Shishido, *Problems*, *supra* note 120, at 341–44.

129. Hamada, *Shareholder's Right*, *supra* note 112, at 63.

130. INABA TAKEO & ŌTANI YOSHIO, SHŌHŌ, YŪGEN-KAISHA-HŌ KAISEI SHI'AN NO KAISETSU [COMMENTARY ON THE COMMERCIAL CODE AND LIMITED LIABILITY CORPORATION ACT REFORM PROPOSAL] 64 (Bessatsu Shōji Hōmu No. 89, Shōjihōmu Kenkyū-kai 1986).

challenging corporate formalities.<sup>131</sup> The second shortcoming is that compelling aggrieved shareholders and their attorneys to bring lawsuits unrelated to the underlying dispute imposed unnecessary burdens on,<sup>132</sup> and arguably brought disrepute to, Japan's justice system. By the 1980s, a consensus had emerged: the law had to be reformed.

## 2. Reform Attempt of the 1980s

The need for some form of withdrawal remedy was identified at least as early as 1951 (for KJs).<sup>133</sup> As the problems of close corporations came to be better understood over the 1970s, many Japanese academics came to the view that reform was necessary.<sup>134</sup> The emerging consensus culminated in one serious attempt at introducing a withdrawal regime for the KJ and the YK via legislation, which took place as part of a comprehensive reform primarily of KJ law. Consultations in 1984<sup>135</sup> culminated in the 1986 Commercial Code and Limited Liability Corporation Act Reform Proposal ("1986

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131. See cases cited in EGASHIRA 2005, *supra* note 103, at 323 n.1. They have not escaped criticism by academics more sympathetic to the plight of these shareholders, including Egashira himself, who criticized the courts for being excessively moralistic. *Id.*

132. See Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 16 (reporting that overburdened judges have called for reform).

133. Komachiya Sōzō, *Kaisei Kabushiki Kaisha Hō Kanzen* [*Submissions on the Reforms to the Law on the KJ*], 15 TŌHOKU HŌGAKU 369, 404 (1951) (proposing a withdrawal remedy as a replacement for the then-newly introduced shareholder right to apply for judicial dissolution).

134. Among the earliest to take up the cause of reform is Hamada Michiyo, who began advocating for a withdrawal right *at will* based on her research on the law of close corporations in the United States in a 1974 book. See HAMADA MICHIO, *AMERIKA Heisa Kaisha Hō: Sono Genjō oyobi Nihon Hō e no Teigen* [*AMERICAN CLOSE CORPORATION LAW: ITS CURRENT STATE AND ITS SUGGESTIONS FOR JAPANESE LAW*] 340–45 (Shōjihōmu Kenkyū-kai 1974). Other scholarly "converts" included Takeuchi Akio, a leading University of Tokyo corporate law scholar. Yazawa Makoto et al., *Shōhō Bukai SHIMPOJIUMU: Kaisha Hō no Konpon Kaisei* [*Corporate Law Subcommittee Symposium: Fundamental Reform of Corporate Law*], 39 SHIHŌ 95, 119–120 (1977) (Statement by Takeuchi Akio); see also Mori Junjirō, *Heisa-kaisha ni okeru Shihai no Iji to Tōka-shihon no Kaishū* [*Maintenance of Control and Recovery of Invested Capital in Closed Corporations*], 56(11) HŌRITSU JIHŌ 23, 25–27 (1984).

135. For the original consultation document, see HŌMU-SHŌ MINJI-KYOKU SANJIKAN-SHITSU [COUNSELLORS' OFFICE, CIVIL AFFAIRS BUREAU, MINISTRY OF JUSTICE], *Taishō (Kōkai, Hi-Kōkai) Kaisha Kubun Rippō oyobi Gappei ni kansuru Mondaiten—Shōwa 59-nen 5-gatsu 9-nichi (Shiryō)* [*Issues on Legislating Separately for Companies Based on Size Distinctions (Open, Closed) and Mergers—9 May 1984 (Materials)*], in TAISHŌ KAISHA KUBUN RIPPŌ-TŌ NO RONTEN—HŌMUSHŌ NO "MONDAITEN" NO KAISETSU TO BUNKEN KAIDAI [ISSUES ON LEGISLATING SEPARATELY FOR COMPANIES BASED ON SIZE DISTINCTIONS, ETC.—COMMENTARY ON THE MINISTRY OF JUSTICE'S "ISSUES" AND LITERATURE REVIEW] 190–208 (Inaba Takeo et al. eds., Bessatsu Shōji Hōmu No. 75, Shōjihōmu Kenkyū-kai 1984).

Reform Proposal”) by the Ministry of Justice.<sup>136</sup> Clause 3-8-a of the 1986 Reform Proposal provides:

In stock corporations [KFs] without marketable share certificates and limited liability corporations [YFs], if the interests of a part of the shareholders or members are dealt with in a significantly unfair manner, the affected shareholders or members shall have a claim as against the corporation for the designation of a purchaser for their shares or membership interests.<sup>137</sup>

Under the proposed regime, the corporation may purchase its own shares but only up to the limit that may be distributed as dividends (Clause 3-8-c). If the person designated as purchaser fails to perform their obligation, or the corporation fails to make a designation within a specified time frame (such as three weeks), the representative director or directors<sup>138</sup> would be deemed the designated purchaser or purchasers with joint and severable liability respectively (Clause 3-8-d and explanatory note).<sup>139</sup>

Amidst incessant debate over the 1986 Reform Proposal’s lack of clarity on important issues,<sup>140</sup> the only attempt at introducing a withdrawal mechanism ended in failure,<sup>141</sup> possibly due to concerns

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136. For the full text of the Reform Proposal, see HÔMU-SHÔ MINJI-KYOKU SANJIKAN-SHITSU [COUNSELORS’ OFFICE, CIVIL AFFAIRS BUREAU, MINISTRY OF JUSTICE], *Shôhō, yûgen-gaisha-hō kaisei shi’an (Shōwa 61-nen 5-gatsu 15-nichi)* [Commercial Code and Limited Liability Corporation Act Reform Proposal (15.05.1986)], in INABA & ÔTANI, *supra* note 130, at 125–42.

137. INABA & ÔTANI, *supra* note 130, at 58.

138. Under Japanese corporate law not all directors *ipso facto* have the power to “represent” (*daihyō*) the corporation, *i.e.*, to act as its legal agent with power to bind the corporation. Directors so empowered are called “representative directors” and are functionally equivalent to managing directors, presidents, or CEOs in other jurisdictions. *See generally* Kaisha-hō, [Companies Act], Law No. 86 of 2005, art. 349 (Japan) (stating the powers of representatives of KFs).

139. INABA & ÔTANI, *supra* note 130, at 58.

140. Hamada observed that the 1986 Reform Proposal did not clearly state which corporate organ, the board of directors or the shareholder meeting, should appoint the designated purchaser, and observed that the issue would be more complex where the corporation itself is the designated purchaser. *See* Hamada Michiyo, *Kabushiki, Mochibun no Kaitori Seikyū-ken: Kaisha-hō Kaisei Shi’an ni okeru sono Kōsō ni tsuite* [The Right to Demand Repurchase of Shares and Membership Interests: On their Conception in the Corporate Law Reform Proposal], 1093 SHÔJI HÔMU 2, 7 (1986) [hereinafter Hamada, *Right to Demand*].

141. Toward the end of 1989, the Commercial Law Subcommittee (*Shôhō-bukai*) determined that it would be too difficult to resolve all the issues covered by the extensive 1986 Reform Proposal together. Subsequently, the Legislative Council prepared a much-reduced reform outline in March 1990 that was later submitted, with few amendments, as the reform bill by the government to the Diet in April 1990. The bill was passed without amendment by both Houses in June 1990, but with the proposed withdrawal reforms completely dropped. *See* Hamada Michiyo, *Shō-kibo Kaisha ni kansuru Rippō-jō no Mondaiten* [Issues in Legislating for Small-scale Corporations], in *Shôhō no Sōten I: Sōsoku, Kaisha* [CONTESTED ISSUES IN COMMERCIAL LAW I: GENERAL PART, CORPORATIONS] 30–31 (Kitazawa Masahiro & Hamada Michiyo eds., Yūhikaku 1993).

over enforcement mechanisms.<sup>142</sup> Thus, notwithstanding academic consensus on the salience of shareholder conflict, the Japanese legislature failed to act.<sup>143</sup>

### 3. Japanese Businesses Chose Close Corporation Forms Without Withdrawal for a Variety of Strategic Reasons

The preceding discussion in Part II.B and Part III has established that withdrawal is essential to the resolution of close corporation disputes. Notably, neither the KK nor YK expressly offered this solution; further, the functional substitutes for a formal system of withdrawal were, at their best, partial and problematic. The mystery deepens when we consider that there were other corporate forms offering withdrawal such as the commercial partnership (*gōmei kaisha*) or limited partnership (*gōshi kaisha*),<sup>144</sup> but which were deeply unpopular by comparison.<sup>145</sup> Thus the final piece of the puzzle: Why then did the Japanese consistently choose to incorporate millions of KKs and YKs?

The short answer is that there were compelling strategic reasons to incorporate as KKs or YKs notwithstanding the absence of a legal withdrawal regime. The first is limited liability. In contrast to the commercial partnership and limited partnership, only KKs and YKs then offered limited liability for all shareholders/members.<sup>146</sup> The

142. Kawamoto made a very brief observation that the withdrawal reforms were dropped over problems with the proposed enforcement mechanism, by which the designated purchaser's failure to pay would result in dissolution of company. Kawamoto Ichirō, *Shōhō, Yūgen-kaisha-hō Kaisei ni tsuite no Kei'i* [A Chronology of the Reform of the Commercial Code and Limited Liability Corporation Act], 856 KIN'YŪ SHŌJI HANREI 12, 14 (1990). Kawamoto was then a member of the Commercial Law Subcommittee involved in refining the 1986 Reform Proposal into a workable legislative agenda.

A detailed analysis and criticism of the proposed enforcement mechanisms (or lack thereof) for the proposed withdrawal remedy was offered by Hamada. Hamada, *Right to Demand*, *supra* note 140, at 3–5. For another pointed critique, see Ōga Yoshimitsu, *Hi-Kōkai Kaisha ni okeru Shōsū-ha Kabunushi, Sha'in no Yokuatsu kara no Kyūsai: Kabushiki, Mochibun no Kaitori Seikyū Seido* [Relief from Oppression of Shareholders/Members in Non-Open Corporations: The Share/Membership Interest Buyout Regime], 10 SHŪDŌ HŌGAKU 275 (1988).

143. Hamada Michiyo, *Heisa-kaisha ni okeru Kabushiki Seido no Kaisei* [Reform of the Share System in Closed Corporations], 963 JURISUTO 48, 53 (1990).

144. These entities will be discussed together with the new GK corporate form below. See *infra* Part IV.A.2.

145. See Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 4 fig.2 (providing a graphical representation of data from the National Tax Agency on the different types of corporate forms in Japan).

146. Pre-Kaisha-hō, companies were not permitted to become unlimited members of commercial partnerships and limited partnerships. Shō-hō, [Commercial Code], Law No. 48 of 1899, art. 55 (Japan) (repealed). In limited partnerships, limited members were expressly prohibited from managing the company or acting as the company's

choice for Japanese business people was *either* limited liability or withdrawal.<sup>147</sup> Corporate forms with full limited liability were consistently preferred, given that the two incorporated partnership forms were greatly outnumbered by Kks as early as 1950 and by Yks by 1955.<sup>148</sup> For the vast majority of businesses in Japan's postwar era, the only practical choice was between the KK and the YK.

Japanese commentators have offered other reasons for the popularity of Kks and Yks. Tax advantages<sup>149</sup> likely played a major role in the "corporatization" (*hōjin-nari*) of businesses in the postwar years, in which businesses previously run as sole proprietorships incorporated *en masse* as close corporations, and almost invariably as Kks or Yks.<sup>150</sup> Another related advantage was the impression of size and social credibility that trading as a KK conveyed.<sup>151</sup>

Hamada gave a more sophisticated account for the popularity of the KK and YK: accounting standards. Surveys she conducted in 1982 revealed that the most common reason for incorporating as KK or YK—"clearer accounting contributes to the optimization of corporate management"<sup>152</sup>—was cited by almost two-thirds of KK and over half of YK respondents.<sup>153</sup> The connection between KK/YK incorporation and accounting lay in Japan's postwar corporate compliance environment. As businesses began incorporating postwar as Kks or Yks *en masse* for tax advantages, they became subject to more exacting mandatory accounting requirements.<sup>154</sup> These corporations came to rely heavily on accounting professionals,<sup>155</sup> with many companies

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representative. Shō-hō, art 156 (repealed). Accordingly, only unlimited members were permitted to manage a commercial/limited partnership, and using a German-style GmbH & Co. KG hybrid such as a YK & Co. limited partnership to provide *de facto* full limited liability for all members including those representing and/or managing the company would have been also out of the question.

147. For reasons set out at text accompanying *supra* note 109, it was highly unlikely that businesspeople would have even considered the question framed as such.

148. Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 4 fig.2 (demonstrating this with National Tax Agency data).

149. See HIROMITSU ISHI, *THE JAPANESE TAX SYSTEM* 171–82 (3d ed., Oxford University Press 2001) (describing the Japanese tax system and the tax advantages it affords to smaller incorporated firms).

150. EGASHIRA 2005, *supra* note 103, at 4 n.7 (noting the role of tax accountants in encouraging incorporations); Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 6 (pointing out that the KK's overwhelming popularity astonished observers).

151. Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 6 (summarizing earlier literature and survey findings).

152. *Cf. id.* at 8 tbl.2 (translating as "better accounting techniques are employed and it promotes the rationalization of our management"). The study discussed by Hamada here is the same as that cited in this Article at *infra* note 153.

153. Kitazawa & Hamada, *supra* note 77, at 30 tbl.13 (reporting that 64.3% of KK respondents and 52.5% of YK respondents cited this reason). The second most popular reason was "increased credibility when dealing with trading partners". *Id.*

154. Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 10–11.

155. *Id.* at 11.

retaining them as corporate advisors.<sup>156</sup> Businesses gradually came to realize that good accounting practices contributed towards business optimization<sup>157</sup> and, in turn, greater business success in KKKs and YKKs and greater social credibility. Businesspeople who chose the KKK, with the strictest applicable accounting standards, benefited from being perceived as “businessmen who are determined to manage a modern enterprise systematically rather than small businessmen who only wish to support their families.”<sup>158</sup>

Note that all the strategic reasons motivating the Japanese to choose corporate forms without withdrawal have one thing in common: none of them related to the close corporation problem. There is also no clear evidence to suggest that ordinary Japanese business participants were even generally aware of the fact that KKKs and YKKs lacked a legal withdrawal regime. It is thus at least a distinct possibility, if not likely, that businesspeople were simply largely unaware of the potential consequences flowing from withdrawal's absence in the presence of shareholder conflicts in close corporations. It is difficult to imagine how a person could be influenced by something that they are unaware of. Accordingly, the fact that businesses in Japan historically overwhelmingly chose to incorporate as corporate forms without any withdrawal regime does not undermine the case (as advanced in Part II.B above) that withdrawal is valuable as the necessary ultimate solution to the close corporation. On the contrary, the fact that partial, functional substitutes for a nonexistent system of withdrawal *in law* came to be used strongly indicates unaddressed demand for withdrawal *in fact*.

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Matters do not appear to have changed significantly since then. The 2005 *Kaisha-hō* still contains no withdrawal provisions applicable to KKKs, including ex-YKKs. However, the *Kaisha-hō* was also a silent revolution in withdrawal, introducing a new corporate form offering limited liability for all members and withdrawal almost as an afterthought.<sup>159</sup> What is this new corporate form, and why did it come to offer withdrawal? This is the subject of the next Part.

#### IV. THE PRESENT: JAPAN'S *GŌDŌ KAISHA* (GK) CORPORATE FORM

The *Kaisha-hō* was epochal for Japanese close corporation law by destroying one venerable close corporation form and creating a new,

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156. Hamada, *Shareholder's Right*, *supra* note 112, at 69 fig.4 (showing that 78.3% of KKKs and 73.6% of YKKs with stated capital of under JPY 100 million retained certified tax accountants [*zeirishi*] or other accounting professionals such as certified public accountants [*kōnin kaikeshi*] in an advisory capacity).

157. Hamada, *Forthcoming Legislative Reform*, *supra* note 75, at 11, 14.

158. *Id.* at 14.

159. *See infra* Part IV.B (discussing the impact of the *Kaisha-hō*).

fledgling one, and for ushering Japan's first withdrawal regime that is applicable to a corporate form offering full limited liability. An analysis of withdrawal in contemporary Japanese close corporation law is inseparable from the still relatively new *Gōdō Kaisha* (GK) corporate form. Accordingly, this Part sets out the GK's legislative origins and surrounding context before Part V launches into a close examination of the finer points of Japan's current withdrawal regime.

### A. The GK as a "Membership Company"

#### 1. The Impetus for the GK

The archetypical close corporation form in Japan today is the relatively new GK,<sup>160</sup> a creature of the *Kaisha-hō*. The GK is not a renamed or modernized YK; rather, it is a legislative invention modeled upon the American limited liability company (LLC).<sup>161</sup> It arose as part of a plan to create a Japanese version of the LLC that would serve as an entity with pass-through taxation following the precedent set by the US LLC. This original concept fell through in the face of opposition from the Ministry of Finance; what was ultimately enacted was the GK, a corporation subject to corporation tax.<sup>162</sup>

In contrast to the YK, which was governed by its own statute supplemented by *mutatis mutandis*<sup>163</sup> application (*jun'yō*<sup>164</sup>) of mainly provisions governing KKs from the *Shō-hō*,<sup>165</sup> the GK is part of a family of corporate forms known as "membership companies."

160. Although the modern KK, which includes ex-YKs that have yet to change corporate forms or dissolve, still make up a large share of close corporations in Japan, I do not discuss them as the *Kaisha-hō* does not offer withdrawal for KK shareholders. See *supra* Part. III.B.

161. Shishido Zen'ichi, *Dai-3-pen Zenchū [Introduction to Part III]*, in 14 KAISHA HŌ KONMENTĀRU: MOCHIBUN KAISHA (1) [COMMENTARY ON THE COMPANIES ACT: MEMBERSHIP COMPANIES (1)] 5, 21 (Kanda Hideki ed., Shōjihōmu 2014) [hereinafter Shishido, *Introduction to Part III*]. The critical difference between GKs and LLCs is the absence of pass-through taxation for the former that so characterized the latter. *Id.*

162. Baum & Goto, *supra* note 75, at 93; Sekiguchi Norihiro & Nishigaki Kengō, *Gōdō-Kaisha ya Yūgen-Sekinin-Jigyō-Kumiai no Jitsumu-jō no Riyōrei to Mondaiten [GKs and J-LLPs: Practical Examples and Issues]*, 80(11) HŌRITSU JIHŌ 18, 18–19 (2008).

163. See, e.g., YK at 19(3)–(7) (applying various *Shō-hō* provisions on restricted-transfer shares *mutatis mutandis*).

164. The verb form, "*jun'yō suru*" is defined as "apply *mutatis mutandis*". *Jun'yō-suru*, JAPANESE LAW TRANSLATION COUNCIL, STANDARD LEGAL TERMS DICTIONARY 152 (Mar. 2019 ed.). *Mutatis mutandis* is in turn defined as "with the necessary changes in points of detail, meaning that matters or things are generally the same, but to be altered when necessary, as to names, offices, and the like." *Mutatis Mutandis*, BLACK'S LAW DICTIONARY (11th ed. 2019).

165. SAKAMAKI, *supra* note 73, at 240 (noting that the YK Act would total over 200 provisions if all the cross-referenced Commercial Code provisions were counted).

## 2. “Membership Companies”: Concept and Design Features

Under the *Kaisha-hō*, the GK together with two historic corporate forms, the incorporated “commercial partnership” with unlimited liability<sup>166</sup> (*gōmei kaisha*)<sup>167</sup> and the incorporated “limited partnership” (*gōshi kaisha*),<sup>168</sup> now comprise a new category of corporation, the “membership companies” (*mochibun kaisha*).<sup>169</sup> Regulated under the current regime primarily by their own separate Part in the *Kaisha-hō*,<sup>170</sup> membership companies are distinguished from Kks in three aspects. First, they are permitted more freedom in contractual ordering in their corporate constitutions.<sup>171</sup> This is facilitated by lower incorporation and related costs; there is no need for the constitution to be notarized,<sup>172</sup> and the registration license fees are also much lower.<sup>173</sup>

Second, the members are not conceptually separated from the corporate organs; in principle they *are* the corporate organ.<sup>174</sup> There are no directors (*torishimariyaku*) or boards of directors (*torishimariyaku-kai*) as such; membership company members, by default, are simultaneously “executive members,” who have executive powers (*gyōmu wo shikkō suru*), as well as “representative members” (*daihyō sha'in*), who have the authority to bind the company.<sup>175</sup> The membership company also has the option of limiting representative powers to specific executive members, and it can do so by designating

166. Cf. Companies Act 2006, c. 46, § 3(4) (U.K.) (defining “unlimited company” in the UK).

167. *Shō-hō*, [Commercial Code], Law No. 48 of 1899, arts. 62–145 (Japan) (repealed).

168. *Id.* arts. 146–164 (repealed).

169. “Membership Company” (in the singular) is the semi-official translation adopted by the Japanese government. *Mochibun kaisha* [Membership Company], JAPANESE LAW TRANSLATION COUNCIL, STANDARD LEGAL TERMS DICTIONARY 276 (Mar. 2019 ed.).

170. *Kaisha-hō* [Companies Act], Law No. 86 of 2005, pt. III (Japan) (containing arts. 575–675, which govern membership company law).

171. Shishido, *Introduction to Part III*, *supra* note 161, at 9–11.

172. *Kaisha-hō*, art. 30(1) (requiring notarization for Kks); Sekiguchi & Nishigaki, *supra* note 162, at 19 (Gks do not need notarization). The cost of notarization is JPY 50,000. *Kōshōnin Tesū-ryō Rei* [Cabinet Order on Notary Fees], Cabinet Order No. 224 of 1993, as amended by Cabinet Order No. 30 of 2015, art. 35.

173. *Tōroku Menkyo-zei Hō* [Registration and License Tax Act], Law No. 35 of 1967, *Beppyō* [Annexed Table] 1, Heading 24 (*Kaisha mata wa Gaikoku Kaisha no Shōgyō Tōki* [Business Registration of Companies or Foreign Companies]), No. 1, Item (i) (Kks: the higher of 0.7% of registered capital or JPY 150,000); Item (ro) (incorporated partnerships and limited partnerships: JPY 60,000); Item (ha) (Gks: the higher of 0.7% of registered capital or JPY 60,000).

174. TAKAHASHI EIJI, *KAISHA HŌ GAISETSU* [PRINCIPLES OF CORPORATION LAW] 281 (2d ed., Chūōkeizasha 2014) [hereinafter TAKAHASHI, PRINCIPLES].

175. *Kaisha-hō*, arts. 590, 599.



them directly or by stipulating procedures for the appointment of one or more representative members in the corporate constitution.<sup>176</sup>

Third, membership companies are close corporations,<sup>177</sup> optimized for small organizations or joint ventures.<sup>178</sup> The personalistic element (*jinteki yōso*) is stronger in membership companies than in the KK.<sup>179</sup> Membership companies are premised on personal trust between the members, and, as a concept, stand in opposition to the KK.<sup>180</sup> The personalistic nature of membership companies is stronger than in analogous organizational forms in other jurisdictions; in contrast with the US limited partnership or LLC,<sup>181</sup> membership company interests may not be publicly traded.<sup>182</sup>

Finally, as Japan's GK has received relatively little attention in the Western language literature, some clarification on terminology is necessary to avoid confusion with the more prominent KK. The word *mochibun*, which is adopted by the legislature as the name of the new category of membership companies (*mochibun kaisha*) in the *Kaisha-hō*, is the Japanese word used for "membership interests" in the three entities.<sup>183</sup> They are not shares or stock (*kabu*), which is the term used for equity interests in the KK.<sup>184</sup> The correct term for members of *mochibun kaisha* is not "shareholder" (*kabu'nushi*), but rather "member" (*sha'in*). Reflecting this, in this Article "member" is *not* used interchangeably with "shareholder," and other membership company-

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176. *Id.* art. 599(3).

177. TAKAHASHI, PRINCIPLES, *supra* note 174, at 281.

178. Shishido, *Introduction to Part III*, *supra* note 161, at 8.

179. Koide Atsushi, *Dai-606-jō* [Article 606], in 14 KAISHA HŌ KONMENTĀRU: MOCHIBUN KAISHA (1) [COMMENTARY ON THE COMPANIES ACT: MEMBERSHIP COMPANIES (1)] 211, 213–15 (Kanda Hideki ed., Shōjihōmu 2014) (explaining how this difference influences the design of the members' withdrawal regime).

180. Shishido, *Introduction to Part III*, *supra* note 161, at 6; see also Koide, *supra* note 179, at 213–14.

181. See generally Mohsen Manesh, *Contractual Freedom Under Delaware Alternative Entity Law: Evidence from Publicly-Traded LPs and LLCs*, 37 J. CORP. L. 555 (2012) (analyzing operating agreements of publicly-traded LLCs and LPs in Delaware). However, a publicly-traded LLC would lose the preferential tax treatment granted to LLCs unless passive income makes up 90% or more of its income. I.R.C., § 7704 (2008); Manesh, *supra* note 181, at 573.

182. Zenichi Shishido, *Legislative policy of alternative forms of business organization: the case of Japanese LLCs*, in RESEARCH HANDBOOK ON PARTNERSHIPS, LLCs AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS 374, 374 (Robert W. Hillman & Mark J. Loewenstein eds., Edward Elgar 2015) ("[T]he [GK] form can be used only for closely held firms in Japan, while, in the United States, the LLC form is available for both closely held and publicly held firms ... the [KK] is the only legal form available for publicly held firms in Japan.") (citation omitted).

183. As well as in the YK prior to forced conversion into Kks. See *supra* notes 70–72 and accompanying text.

184. Aizawa Tetsu & Kōriya Daisuke, *Mochibun Kaisha* [Membership Companies], in RITSUAN TANTŌSHA NI YORU SHIN-KAISHA HŌ NO KAISETSU [THE DRAFTSMEN'S COMMENTARY ON THE NEW COMPANIES ACT] 153, 153 n.1 (Aizawa Tetsu ed., Bessatsu Shōji Hōmu No. 295, Shōjihōmu 2006).

specific terminology such as “executive member”—instead of “director”—are used accordingly.

### B. *Withdrawal: A Semi-Accidental but Defining Feature*

The most important feature common to the three membership company types is the availability of withdrawal. All three types of membership companies are subject to the same basic withdrawal regime set out in Articles 606 to 613.<sup>185</sup> The basic framework had existed for over a century: under the Commercial Code of 1899, members of commercial partnerships and limited partnerships had withdrawal rights.<sup>186</sup> By consolidating the old Commercial Code withdrawal provisions and making them applicable to membership companies in general, the *Kaisha-hō* therefore extended the withdrawal regime to cover the GK. Thus, as a membership company, the GK offers both withdrawal *at will* (Part V.A below) and withdrawal on grounds (Part V.B below).

In contrast with the reform efforts of the 1980s to introduce withdrawal into the KK and YK,<sup>187</sup> a key document from the reform period reveals only the most cursory concern with *why* precisely the GK should be equipped with withdrawal remedies. In the *Preliminary Draft Principles for the Modernization of the Corporate Law Regime*, approved on October 22, 2003<sup>188</sup> (*Preliminary Draft Principles*), it was taken for granted that the proposed new corporate form (that became the GK) would incorporate features of the legacy incorporated partnership form, including withdrawal.<sup>189</sup> The rationale given for withdrawal is to provide the means by which a member could withdraw their investment; it takes the place of a transfer of shares or

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185. Supplemented by special provisions applicable only to the GK in *Kaisha-hō* [Companies Act], Law No. 86 of 2005, arts. 635–36 (Japan).

186. *Shō-hō* [Commercial Code], Law No. 48 of 1899, arts. 84, 147 (Japan) (repealed).

187. See *supra* Part III.C.2.

188. *Hōsei Shingikai Kaishahō* (Gendaika Kankei) Bukai [Corporate Law (Modernization) Subcommittee, Legislative Council, Ministry of Justice], *Kaisha Hōsei no Gendaika ni kansuru Yōkō Shi'an* [Preliminary Draft Principles for the Modernization of the Corporate Law Regime] (Oct. 22, 2003), <http://www.moj.go.jp/content/000071772.pdf> (last visited Feb. 23, 2020) [<https://perma.cc/66UK-VQAV>] (archived Aug. 19, 2020) [hereinafter *Preliminary Draft Principles*]. This document was approved at the 15<sup>th</sup> Meeting of the Corporate Law (Modernization) Subcommittee (*Kaishahō* (Gendaika Kankei) Bukai) of the Legislative Council of the Ministry of Justice (*Hōsei Shingikai*). This document, which offers up to three options for each important point of reform (called “Proposal A”, “Proposal B”, and “Proposal C” and so on), was later opened for public consultation and feedback (“public comment” in the Japanese context). Based on the feedback received, a reworked version would be submitted for approval by the full Legislative Council, the final version of which would be the basis for the Ministry of Justice’s legislative draftspeople’s work on the actual draft statutory provisions for the bill.

189. See *Preliminary Draft Principles*, *supra* note 188, dai-6-bu, 1 chū 1(1)–(2).

membership interests, as would otherwise be the case in KKs or YKs.<sup>190</sup>

The only policy question related to the withdrawal regime that was opened for public consultation and feedback was on the relatively technical issue of creditor protection.<sup>191</sup> Even from a relatively early stage of the reform process, the subject of *whether* the GK should have withdrawal was never up for debate, only the *how*.<sup>192</sup>

The exclusive focus on “how” instead of “why” was maintained in subsequent documents. The finalized *Principles for the Modernization of the Corporate Law Regime* adopted on February 9, 2005<sup>193</sup> (*Principles*) did not touch on the specific rationale for making withdrawal available for the GK, but stated plainly that “notwithstanding the provisions of the corporate constitution, members of GKs shall have the right to withdraw if there are unavoidable grounds.”<sup>194</sup> The *Principles* also provided that the withdrawing member shall have the right to a refund, albeit to creditor protection rules and procedures where the GK has insufficient distributable surplus to make the refund.<sup>195</sup> In his authoritative commentary on the *Principles*,<sup>196</sup> Egashira Kenjirō mentioned only that the GK member’s right to withdraw where unavoidable grounds exist follows from restrictions on the recovery of investment via transfer of membership interests, and that the issue was already

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190. *Id.* dai-6-bu, 1 chū 1(2) chū (“The regime shall not guarantee the recovery of investment via transfer [of ownership interests].”) (translated); Hōmu-shō Minji-kyoku Sanjikan-shitsu [Counsellors’ Office, Civil Affairs Bureau, Ministry of Justice], Kaisha Hōsei no Gendaika ni kansuru Yōkō Shi’an Hosoku Setsumei [Supplementary Explanations to the Preliminary Draft Principles for the Modernization of the Corporate Law Regime] (Oct. 2003), at 98, <http://www.moj.go.jp/content/000071773.pdf> (last visited Feb. 23, 2020) [<https://perma.cc/E54G-FYCL>] (archived Aug. 19, 2020) [hereinafter “MOJ Supplementary Explanations”] (connecting the new corporate form’s emphasis on the relationship between members with the decision to specify withdrawal (*taisha*) as the means of recovery of investment).

191. Two options were offered for public feedback, with Proposal A being a procedure akin to capital reduction, and Proposal B being akin to liquidation. See Preliminary Draft Principles, *supra* note 189, Dai-6-bu, 1 chū 2(5); MOJ Supplementary Explanations, *supra* note 190, at 99.

192. The “how” question was answered by special additional rules specific to the GK that apply on top of the general rules for membership companies. See Aizawa & Kōriya, *supra* note 184, at 165.

193. The Legislative Council of the Ministry of Justice adopted the *Principles* at their plenary meeting. For the full text as adopted, see Hōsei Shingikai [Legislative Council, Ministry of Justice], Kaisha Hōsei no Gendaika ni kansuru Yōkō-an [Draft Principles for the Modernization of the Corporate Law Regime] (Feb. 9, 2005), [http://www.moj.go.jp/shingi1/shingi\\_050209-1-1.html](http://www.moj.go.jp/shingi1/shingi_050209-1-1.html) (last visited Feb. 23, 2020) [<https://perma.cc/EA25-NUHL>] (archived Aug. 19, 2020) [hereinafter Finalized Draft Principles].

194. *Id.* dai-3-bu, dai-2, 5(1).

195. *Id.* dai-3-bu, dai-2, 5(2).

196. Technically, the commentary was on the draft *Principles* (i.e., pre-formal adoption by the Legislative Council), but for this Article’s purposes, the contents are the same.

addressed in the *Preliminary Draft Principles*.<sup>197</sup> In a similar vein, the official draftsmen's commentary on the *Kaisha-hō* provided a wealth of detail on the "how," but was completely silent on the "why."<sup>198</sup>

From the law reform documents, it appears that once the decision was made to create the GK in the image of the Meiji-era incorporated partnership, that the GK would come packaged with mandatory withdrawal rights was a foregone conclusion.<sup>199</sup> Ultimately, the advent of Japan's first withdrawal regime for close corporations offering full limited liability would be the semiaccidental but profound consequence of the conceptualization and creation of the GK as a member of the "membership company" family.

Going forward, the story of withdrawal in Japan is the story of withdrawal *in the GK*. The GK is not without its challenges; with former YKs converted automatically into KKs post-*Kaisha-hō*,<sup>200</sup> the steady rate of new KK incorporations,<sup>201</sup> and the slow start in GK incorporations, the status quo in which the overwhelming majority of closely held businesses remain KKs is likely to continue for some time. Yet, the *legal* significance of the GK is clear—it is the sole close corporation form with growth potential that provides a legal framework for withdrawal. Even if the withdrawal remedies offered by the GK presently have little direct or immediate impact on the closely held businesses currently incorporated as KKs, if history and recent trends are any guide, the GK seems set to grow in popularity over time.<sup>202</sup>

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197. Egashira Kenjirō, "Kaisha Hōsei no Gendaika ni kansuru Yōkō-an" no Kaisetsu [Commentary on the "Draft Principles for the Modernization of the Corporate Law Regime"], in KAISHA HŌSEI GENDAIKA NO GAIYŌ [OUTLINE OF THE MODERNIZATION OF CORPORATE LAW] 91 (Bessatsu Shōji Hōmu Henshūbu ed., Shōjihōmu 2005) (referring to the Preliminary Draft Principles, *supra* note 188, dai-6-bu, 1 chū 1(2)). Egashira also noted that the Finalized Draft Principles (*supra* note 193) adopted Proposal B in the Preliminary Draft Principles on creditor protection procedures. *Id.*

198. Aizawa & Kōriya, *supra* note 184, at 162, 164–65.

199. See text accompanying *supra* notes 187–198 (explaining why the GK would logically have a withdrawal remedy based on the events leading up to its creation).

200. See *supra* note 80 and accompanying text.

201. See *infra* note 279 and accompanying text. It is impossible to determine what percentage of new incorporations are by closely held businesses given the lack of detailed breakdowns in the government data.

202. See *infra* Table 1.

V. THE PRESENT: THE LAW OF WITHDRAWAL (*TAISHA*) AS APPLIED TO  
THE GK

A. *Withdrawal at Will*

1. General

Article 606, Paragraph 1 provides:

Each member may withdraw from the membership company at the end of the fiscal year if the membership company's duration of corporate existence is not specified in the corporate constitution, or is specified in the corporate constitution as the lifetime of a particular member. In such cases, each member [who seeks withdrawal] must give notice of intention to withdraw at least six months in advance.<sup>203</sup>

The *raison d'être* for withdrawal at will—also described as withdrawal by advance notice (*yokoku ni yoru taisha*)—is that in companies with neither a defined duration of existence nor withdrawal, there is a risk that it would be against the public interest to bind members so harshly to the corporate enterprise.<sup>204</sup> Similarly, companies that would exist for the lifetime of a particular member can be unduly restrictive for the members. In such companies, both the member whose lifetime is defined as the company's duration of existence as well as other members may have recourse to withdrawal under Article 606, Paragraph 1.<sup>205</sup>

A member needs no reason to invoke withdrawal under this Paragraph.<sup>206</sup> According to prevailing opinion, the notice of intent to withdraw should be addressed to the representative member.<sup>207</sup> The purpose of the six months' minimum advance notice requirement is twofold: to simplify accounting and to give due regard to the interests of the company.<sup>208</sup>

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203. Kaisha-hō [Companies Act], Law No. 86 of 2005, art. 606(1) (Japan).

204. MATSUMOTO JŌJI, NIHON KAISHA HŌ RON [ON JAPANESE CORPORATE LAW] 556 (Ganshōdōshoten 1929).

205. Koide, *supra* note 179, at 216–17.

206. *Cf.* Kaisha-ho, art. 606(3) (allowing withdrawal at any time for “unavoidable grounds”); Koide, *supra* note 179, at 216–17; Kosemura Kunio, § 84, in I *Shin-pan Chūshaku Kaisha Hō: Kaisha Sōsoku, Gōmei-Kaisha, Gōshi-Kaisha* [CORPORATE LAW COMMENTARY, NEW EDITION: GENERAL PRINCIPLES, INCORPORATED COMMERCIAL PARTNERSHIPS, LIMITED PARTNERSHIPS] 303, 306–07 (Ueyanagi Katsurō, Ōtori Tsuneko & Takeuchi Akio eds., Yūhikaku 1985).

207. ŌSUMI KEN'ICHIRO & IMAI HIROSHI, 1 KAISHA HŌ RON JŌKAN [1 ON CORPORATE LAW] 94 (3d ed., Yūhikaku 1991); Koide, *supra* note 179, at 217.

208. Koide, *supra* note 179, at 217–18 (also noting that the six months' requirement may also be construed as a creditor protection measure); Kosemura, *supra* note 206, at 306.

## 2. Deviation by Contract

Withdrawal at will is a default rule that membership companies are free to deviate from by express provision in their corporate constitutions (Article 606, Paragraph 2).<sup>209</sup> The precise scope of permissible deviations under this Paragraph is an open question. One unresolved issue is whether, in the absence of contrary provision in the constitution, the six months' minimum notice requirement can be waived by the company.<sup>210</sup> Another issue is whether withdrawal at will can be excluded completely for a set period of time, but here the legislative draftsman provides a tentative answer in the affirmative.<sup>211</sup>

Finally, deviation from the default rule of withdrawal at will by constitutional provision is subject to the mandatory standard that withdrawal on "unavoidable grounds" cannot be eliminated (Article 606, Paragraph 3),<sup>212</sup> and it is this to which the analysis now turns.

### B. *Withdrawal on "Unavoidable Grounds"* (yamu wo enai jiyū)

Article 606, Paragraph 3 provides: "Notwithstanding the two Paragraphs above, each member may withdraw at any time if an unavoidable ground exists."<sup>213</sup> The significance of this provision is twofold. First, withdrawal on unavoidable grounds requires no advance notice and takes effect immediately upon communication of the exiting member's intent to withdraw.<sup>214</sup> The scope of this remedy delimits the range of situations under which a member may seek immediate relief. Second, Paragraph 3 circumscribes the degree of freedom of the company to restrict withdrawal rights.<sup>215</sup> There is consensus that there may be no provision in the corporate constitution that would hinder the freedom of the member to trigger withdrawal for unavoidable grounds at any time, making Article 606, Paragraph 3 a mandatory provision.<sup>216</sup> Therefore, the extent to which the member's

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209. There is, however, an influential strand of academic opinion that considers it to be a semimandatory rule. See Koide, *supra* note 179, at 219 (citing sources relevant to this proposition).

210. See *id.* at 218–19 (summarizing both arguments for and against and preferring the position that does not permit the company to waive the notice requirement).

211. Aizawa & Kōriya, *supra* note 184, at 162.

212. Kaisha-hō, [Companies Act], Law No. 86 of 2005, art. 606(3) (Japan).

213. *Id.*

214. Koide, *supra* note 179, at 221; Kosemura, *supra* note 206, at 307; ŌSUMI & IMAI, *supra* note 207, at 95.

215. See *infra* note 216 and accompanying text.

216. Koide, *supra* note 179, at 219, 225; Kosemura, *supra* note 206, at 309–10; Ōta Minoru, *Mochibun-kaisha no Sha'in no Ka'nyū to Taisha* [Joining and Exit of

right to withdraw is guaranteed is determined by the scope of unavoidable grounds.

As the operative concept, unavoidable grounds requires elaboration. Unfortunately, the legislative draftsmen's commentary of the *Kaisha-hō* is far from helpful on this point:

As to “unavoidable grounds,” it is not sufficient that the member in question has changed his mind. The circumstances on which the creation of the corporate constitution, the entry of the specific member, or the initial formation of the company were premised must have changed so significantly that it has become impossible to continue on as a member according to the original agreement.<sup>217</sup>

There is only one published case since the *Kaisha-hō* went into force that touches on unavoidable grounds. This case was not strictly in the context of a GK, but rather a special corporate form for judicial scriveners<sup>218</sup> that applies provisions of the *Kaisha-hō* relevant to membership companies (including Article 606) *mutatis mutandis* to the corporate form and its members.<sup>219</sup> The company commenced expulsion proceedings against the plaintiff,<sup>220</sup> whereupon the plaintiff gave notice of their intention to withdraw on unavoidable grounds.<sup>221</sup> In a decision upheld by the Tokyo High Court,<sup>222</sup> the Tokyo District Court held that a *shihō shoshi hōjin* is founded on a “relationship of mutual trust between its members”; at the point in time the plaintiff gave notice of intent to withdraw, the “relationship of trust between the plaintiff and the other members had already been lost.”<sup>223</sup> Hence,

*Membership Companies' Members*], in I KAISHA HŌ TAIKEI: KAISHA HŌSEI, KAISHA GAIKON, SETSURITSU [COMPENDIUM ON CORPORATE LAW: THE CORPORATE LAW SYSTEM, CORPORATE LAW THEORY, FORMATION] 348, 354 (Egashira Kenjirō & Monguchi Masahito eds., Seirinshoin 2008). However, the precise extent to which the scope of “unavoidable grounds” can be narrowed by contract is debatable. See *infra* Part V.B.

217. Aizawa & Kōriya, *supra* note 184, at 162.

218. *Shihō shoshi* are a type of legal professional separate and distinct from the *bengoshi*; they perform some of the functions that would be exclusively performed by attorneys-at-law or solicitors in other jurisdictions such as small civil claims, preparation of legal documents, and registration of land and corporate matters. See, e.g., *Shiho-shoshi Profile*, NIHON SHIHŌ SHOSHI-KAI RENGŌKAI [Japan Federation of Shihō-shoshi's Associations], <http://www.shiho-shoshi.or.jp/html/global/english/index.html> (last visited Feb. 23, 2020) [https://perma.cc/AY9T-RVE3] (archived Aug. 19, 2020) (using the term “solicitor” to describe themselves). *Shihō shoshi* may incorporate using a special legal form (*shihō shoshi hōjin*) but it does not come with limited liability. See *Shihō shoshi-hō* [Judicial Scriveners Act], Law No. 197 of 1950, art. 38 (Japan).

219. *Shihō shoshi-hō*, art. 46(2).

220. A membership company may commence court proceedings to expel a member by resolution of a majority of the members (excluding the member subject to the expulsion). *Kaisha-hō*, [Companies Act], Law No. 86 of 2005, art. 859 (Japan).

221. See *infra* notes 222–223.

222. Tōkyō Kōtō Saibansho [Tokyo High Ct.] Feb. 24, 2010, 591 Tōki Jōhō 125, 125–26 (Japan).

223. Tōkyō Chihō Saibansho [Tokyo Dist. Ct.] Oct. 5, 2009, 591 Tōki Jōhō 126, 128 (Japan).

the notice of intent to withdraw was properly founded on unavoidable grounds.<sup>224</sup>

Commentators on withdrawal in the GK are concerned primarily with the extent to which “unavoidable grounds” may be narrowed by contract, that is, the concept’s absolute mandatory minimum content. Influenced by the United States’ experience with LLCs, multiple commentators have stressed the importance of contractual freedom in internal corporate ordering.<sup>225</sup> As a restraint on that freedom, the scope of unavoidable grounds is therefore of great concern and practical relevance. There is some agreement as to a minimum core for the concept of “unavoidable grounds.” At a bare minimum, severe conflict over corporate management resulting in deadlock and “improper squeeze-out” (*futō na shimedashi kōi*) of members<sup>226</sup> must be recognized as “unavoidable grounds.”<sup>227</sup>

Beyond this very narrow consensus on deadlock and squeeze-outs, the legal position remains uncertain as to the scope of “unavoidable grounds.”

In contrast with the situation pre-*Kaisha-hō*, modern commentators seem to agree that the scope of “unavoidable grounds” should take into consideration matters beyond the member’s personal circumstances.<sup>228</sup> In particular, Shishido Zen’ichi takes the position that the *default* provision for companies without contrary provision by contract must be a broad withdrawal right that recognizes a wide range of “unavoidable grounds,” including the personal circumstances of the member; this is because the purpose of Article 606, Paragraph 3, a mandatory provision, is to safeguard the members’ freedom to

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224. *Id.*

225. Ōsugi Ken’ichi, *LLC-seido no Dōnyū* [Introduction of the LLC Regime], 56 KIGYŌ KAIKEI 206, 206–09 (2004); Shishido Zen’ichi, *Gōdō Gōben-Kaisha* [GK Joint Ventures], in MAEDA SHIGEYUKI-SENSEI KOKI KINEN: KIGYŌ HŌ, KIN’YŪ HŌ NO SHIN-CHŌRYŪ [FESTSCHRIFT IN CELEBRATION OF MAEDA SHIGEYUKI’S 70TH BIRTHDAY: NEW TRENDS IN ENTERPRISE LAW AND FINANCE LAW] 211, 220ff (Koide Atsushi, Kozuka Sōichirō & Gotō Gen eds., Shōjihōmu 2013) [hereinafter Shishido, *GK Joint Ventures*].

226. This ground is never elaborated upon in the literature on withdrawal.

227. Shishido, *GK Joint Ventures*, *supra* note 225, at 235; Egashira Kenjirō, Ōsugi Ken’ichi, Niinomi Hiroshi, Itō Tsuyoshi & Kuroda Yutaka, *Zadankai: Gōdō Kaisha-tō no Jittai to Kadai (jō)* [Panel Discussion: The Reality and Issues of GKs, etc.], 1944 SHŌJI HŌMU 6, 17–18 (2011) (Statement by Ōsugi Ken’ichi) [hereinafter Egashira, Ōsugi, Niinomi, Itō & Kuroda, *Panel Discussion*]. Both sources point out that the situations contemplated may also suffice as grounds for judicial dissolution (on unavoidable grounds).

228. See, e.g., Egashira, Ōsugi, Niinomi, Itō & Kuroda, *Panel Discussion*, *supra* note 227, at 17 (arguing that when determining if unavoidable grounds are present, not only should the circumstances of the member be considered, but also those of the company, which would after all be affected by the member’s withdrawal).



withdraw.<sup>229</sup> In a later work,<sup>230</sup> Shishido made the following three points. First, family enterprises should have weak exit rights.<sup>231</sup> Second, opportunism in venture capital-funded businesses should be kept in check by the threat of exit.<sup>232</sup> Third, and in quasi-partnership-like<sup>233</sup> businesses where all members participate in management, the strength of exit rights should be left to negotiation,<sup>234</sup> but that neither excessively rigid mandatory rules nor unlimited freedom of contract would be desirable for efficient bargaining outcomes.<sup>235</sup> Shishido's position, while seemingly against generous *mandatory* withdrawal rights, is nonetheless consistent with strong withdrawal rights that, without being mandatory, are not easy to contract out of carelessly.<sup>236</sup>

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229. Shishido, *Introduction to Part III*, *supra* note 161, at 15; see also Shishido Zen'ichi, *Gōdō-Kaisha no Taisha-in no Mochibun Hyōka: Jōto Seigen Kabushiki no Hyōka to no Hikaku* [Valuation of the Membership Interests of Withdrawing Members from the GK: A Comparison with the Valuation of Shares with Transfer Restrictions], in KIGYŌ HŌ NO GENZAI: AOTAKE SHŌICHI-SENSEI KOKI KINEN [ENTERPRISE LAW'S PRESENT: Festschrift in Celebration of Aotake Shōichi's 70th Birthday] 427, 435 (Deguchi Masayoshi, Yoshimoto Ken'ichi, Nakajima Hiromasa & Tanabe Hiroyasu eds., Shinzansha 2014) [hereinafter Shishido, *Valuation*].

230. The core idea in this work is that exit mechanisms (which include not only withdrawal but also dissolution) and compensation claims (*i.e.*, damages claims for breach of duty of loyalty (*chūjitsu gimu*) against KK directors and membership company members) serve as substitutes for each other. Shishido Zen'ichi, *Hi-kōkai Kigyō ni okeru Dōki-dzuke Kōshō: Chūjitsu Gimu to Taishutsu-ken no Daitai-sei no Kanten kara* [Incentive Bargaining in Closed Enterprises: From the Perspective of Substitutability of the Duty of Loyalty and Exit Rights], in KAISHA-HŌ NO TŌTATSU-TEN TO TENBŌ: MORI JUNJIRŌ-SENSEI TAISHOKU KINEN RONBUNSHŪ [THE ULTIMATE GOAL AND OUTLOOK FOR CORPORATE LAW: Festschrift for the Occasion of Professor Mori Junjirō's Retirement] 209, 215–17 (Tokumoto Minoru, Jo Chibun, Satō Makoto, Tanaka Shin'ichi & Kasahara Takeaki eds., Hōritsubunkasha 2018) [hereinafter Shishido, *Incentive Bargaining*].

231. *Id.* at 216.

232. *Id.* at 216–17.

233. The exact word used was *kyōdō jigyo-gata*, but it is functionally most similar to the classic, quasi-partnership close corporation.

234. Shishido, *Incentive Bargaining*, *supra* note 230, at 216.

235. *Id.* at 223.

236. Different sub-types of close corporations have different needs, and mandatory rules may create difficulties. Nonetheless, it is easier for minorities to selectively contract out of existing rights and solutions than it is to create them from scratch by contract, especially those based on legal standards that takes into account a range of facts and circumstances. A legal standard covering both fault and no-fault scenarios that are difficult, if not impossible, to foresee and plan for *ex ante* also prevents *ex ante* contractual arrangements by majorities that facilitate later opportunism. See generally Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 YALE L.J. 2032 (2012) (discussing the concept of “altering rules” that govern how parties contract around a default).

### C. Effect of Withdrawal

A member who has exercised the right to withdrawal at will ceases to be a member at the end of the fiscal year.<sup>237</sup> For withdrawal on unavoidable grounds, withdrawal takes effect immediately upon the member's communication of intent to withdraw to a representative member of the company.<sup>238</sup> With the termination of status as a member of a GK, any rights and obligations pertaining to membership or management of the GK as between the now ex-member and the GK are also dissolved—save one.<sup>239</sup> Article 611, Paragraph 1 provides that the withdrawn member is also entitled to the “refund” of her membership interest (*mochibun no haraimodoshi*).<sup>240</sup> Note that despite the *functional* similarity between refund and buyout, the word for “refund” (*haraimodoshi*) is specific to the membership company context<sup>241</sup> and is not used interchangeably with “buyout” (*kaitori*) in Japanese legal language.<sup>242</sup> In this Article, the word “refund” is used exclusively when writing in the Japanese membership company context.

Regardless of the form of the member's capital contribution, the member is entitled to a monetary refund.<sup>243</sup> The only party against whom the refund claim can be enforced is the company, not any of its (remaining) members.<sup>244</sup> As monetary sums are involved, next up is the subject of valuation.

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237. This is implicit from *Kaisha-hō*, [Companies Act], Law No. 86 of 2005, art. 606(1) (Japan) (governing voluntary withdrawal by members).

238. Koide, *supra* note 179, at 221.

239. The situation is different for the other two membership companies; withdrawn members continue to be liable in some respects for a period of two years. *Kaisha-hō*, art. 612(1)–(2); *see also* RONTEN KAISETSU SHIN-KAISHA HŌ: SENMON NO MICHISHIRUBE [COMMENTARY ON THE NEW COMPANIES ACT: A THOUSAND-QUESTION GUIDE] 590 (Aizawa Tetsu, Hadama Masami & Kōriya Daisuke eds., Shōjihōmu 2006) (explaining why Article 612 does not apply to ex-GK members) [hereinafter RONTEN KAISETSU].

240. *Kaisha-hō*, art. 611(1).

241. The term only appears in *Kaisha-hō* provisions governing membership companies and not in the general or KK-specific provisions.

242. *Cf.* *Kaisha-hō*, art. 140 *et seq.* (using *kaitori* and variants thereof in the context of purchase of restricted-transfer shares in a KK); *id.* at art. 785 *et seq.* (same in the context of appraisal rights in the KK).

243. *Id.* art. 611(3).

244. This is implicit; there is nothing in the literature that even suggests that any person other than the company may—or should—be liable to pay the refund. There is also a functional similarity between stock repurchases by a KK and the payment of a refund of a withdrawn member's membership interest by a membership company. *See* Kōriya Daisuke & Hosokawa Mitsuru, *Mochibun Kaisha no Keisan* [Membership Company Accounting Matters], in RITSUAN TANTŌSHA NI YORU SHIN-KAISHA HŌ KANKEI HŌMUSHŌ-REI NO KAISETSU [THE DRAFTSMEN'S COMMENTARY ON THE MINISTRY OF JUSTICE ORDINANCES RELATING TO THE NEW COMPANIES ACT] 165 (Aizawa Tetsu ed.,

### E. Valuation

To calculate the refund quantum corresponding to the withdrawing member's membership interest, a valuation of the company must be performed.<sup>245</sup>

#### 1. Default Provision

On the critical subject of valuation, the *Kaisha-hō* offers little concrete guidance. Article 611, Paragraph 2 provides: "Accounting as between the member who has exited and the membership company shall be conducted on the basis of the company's asset situation as at the time of exit."<sup>246</sup>

Per the legislative draftsmen, the valuation should be based on "the mark-to-market valuation of the assets and liabilities of the company on a going concern basis, with future earnings and other factors taken into consideration."<sup>247</sup> However, this short statement does not settle the longstanding debate in academic literature.<sup>248</sup> The prevailing opinion favors valuing the company as a going concern.<sup>249</sup> A substrand of this takes the position that this should not be on a book value basis, as in a profit and loss statement; rather, without undervaluing assets or overvaluing liabilities, revaluation of fixed assets (within appropriate boundaries) is permitted, as is the inclusion of intangibles.<sup>250</sup> More recently, support has emerged for an approach that disregards book value in favor of using, in principle, only discounted cash flow (DCF).<sup>251</sup>

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Bessatsu Shōji Hōmu No. 300, Shōjihōmu 2006). This supports the position that only the company is liable to the withdrawn member in respect of the refund. If the GK fails to take the necessary steps to pay, the withdrawn member may be able to apply for the GK to be judicially dissolved. See Aizawa & Kōriya, *supra* note 184, at 165.

245. *Kaisha-hō*, art. 611(1)–(2); RONTEN KAISETSU, *supra* note 239, at 589.

246. *Kaisha-hō*, art 611(2). Note that I use "exited" and "exit" in lieu of "withdrawn" and "withdraw" because the original Japanese term *taisha* is broader than withdrawal as I define and use in this Article.

247. RONTEN KAISETSU, *supra* note 239, at 589.

248. See *infra* notes 249–251 and accompanying text.

249. See Matsumoto Nobuko, *Dai-611-jō* [Article 611], in 14 KAISHA HŌ KONMENTĀRU: MOCHIBUN KAISHA (1) [COMMENTARY ON THE COMPANIES ACT: MEMBERSHIP COMPANIES (1)] 252, 263 (Kanda Hideki ed., Shōjihōmu 2014) and references cited therein.

250. *Id.* at 263; ŌSUMI & IMAI, *supra* note 207, at 100–01 n.2.

251. Summarized in Matsumoto, *supra* note 249, at 263 and Shishido, *Introduction to Part III*, *supra* note 161, at 13.

Judicial precedents are generally consistent with a going concern approach to valuation. The leading case,<sup>252</sup> which was decided by the Supreme Court in 1969, concerned not a company, but rather a cooperative enterprise regulated under a specific law on cooperatives<sup>253</sup> with a provision similar to the *Kaisha-hō*'s Article 611, Paragraph 2.<sup>254</sup> The Supreme Court held that:

In general, the valuation of the cooperative's assets, on which accounting of the exiting cooperative member's membership interest would be based, should not be performed based on the so-called book value that is used for purpose of calculating the cooperative's profit and loss. Instead, the valuation should be performed on the premise that (1) the cooperative would operate the business as a going concern, and (2) the business would be sold in its entirety on the most advantageous terms.<sup>255</sup>

Subsequent reported decisions in the lower courts from the 1980s have generally followed the Supreme Court's lead.<sup>256</sup>

The going concern approach generally adopted by the courts should not be conflated with DCF valuation.<sup>257</sup> Importantly, Japan experienced an economic bubble that resulted in extremely high land prices, especially towards the end of the 1980s.<sup>258</sup> Inflated land prices played an important role in the reported cases, as the main point of dispute was over the valuation of land forming part of the assets of the cooperative or company.<sup>259</sup> Without exception, the net asset value of the entity in question was greater than its DCF valuation.<sup>260</sup> In one

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252. Saikō Saibansho [Sup. Ct.] Dec. 11, 1969, 23(12) MINSHŪ 2447 (Japan), [http://www.courts.go.jp/app/files/hanrei\\_jp/974/051974\\_hanrei.pdf](http://www.courts.go.jp/app/files/hanrei_jp/974/051974_hanrei.pdf) (last visited Feb. 23, 2020) [<https://perma.cc/U359-CKFS>] (archived July 13, 2020).

253. Specifically, the *Chūshō Kigyō-tō Kyōdō Kumiai Hō* [Small and Medium-Sized Enterprise Cooperatives Act], Law No. 181 of 1949 [hereinafter SME Cooperatives Act]. For an overview of cooperative laws in Japan, see Akira Kurimoto, *Japan, in INTERNATIONAL HANDBOOK OF COOPERATIVE LAW* 503 (Dante Cracogna, Antonio Fici & Hagen Henry eds., Springer 2013).

254. Compare SME Cooperatives Act, art. 20(2) (providing that the valuation of the equity interest of a withdrawn cooperative member shall be conducted based on the cooperative's assets as of the end of the business year in which withdrawal occurred) with *Kaisha-ho*, [Companies Act], Law No. 86 of 2005, art. 611(2) (Japan) (providing that valuation of a withdrawn GK member's equity interest shall be conducted based on the asset position of the GK at the time of withdrawal).

255. Saikō Saibansho [Sup. Ct.] Dec. 11, 1969, 23(12) Minshū 2447 (Japan); see also Matsumoto, *supra* note 249, at 264 (analyzing the Supreme Court's decision).

256. See, e.g., Kōbe Chihō Saibansho [Kobe Dist. Ct.] Aug. 29, 1986, 1222 HANREI JIHŌ [HANJI] 135 (Japan); Nagoya Chihō Saibansho [Nagoya Dist. Ct.] Sept. 29, 1987, 1264 HANREI JIHŌ [HANJI] 128 (Japan). Both were commercial partnership (*gōmei kaisha*) cases.

257. Shishido, *Introduction to Part III, supra* note 161, at 14.

258. See Robert L. Cutts, *Power from the Ground Up: Japan's Land Bubble*, 68 HARV. BUS. REV. 164, 168–69 (1990) (describing the impact of inflated land values on corporations).

259. Shishido, *Valuation, supra* note 229, at 428 n.3.

260. Shishido, *Introduction to Part III, supra* note 161, at 14.

exceptional case from 1995, to avoid an asset bubble-influenced valuation that was disproportionately large compared to the company's earnings, the Tokyo District Court adopted a weighted average of the DCF and net asset value figures.<sup>261</sup> Taking the historical context into consideration, Shishido argues that the going concern approach laid down in the 1969 Supreme Court decision should not be construed as a general requirement for DCF valuation; instead, the valuation can be on either the DCF or net asset value basis, whichever is higher. Further, he posits that valuation on a net asset value basis should be based on both the market value of the business sold as a whole and the most advantageous terms possible, and not the book value or liquidation value.<sup>262</sup>

## 2. Provision in Corporate Constitution

Opinion is divided on whether Article 611, Paragraph 2 is a mandatory provision, and if so, the scope of mandatory regulation. The legislative draftsmen appear to contradict themselves on this point. On the one hand, they take the position that the *Kaisha-hō*'s provisions on membership companies are generally mandatory unless the Act itself expressly permits deviation by provision in the corporate constitution.<sup>263</sup> On the other hand, the draftsmen appear to accept, without elaboration, that where the company has included provisions on valuation in the corporate constitution those provisions should be followed<sup>264</sup>—despite the absence of any *Kaisha-hō* provision within Article 611 permitting deviation. A number of academic commentators have also expressed uncertainty on the subject,<sup>265</sup> although Shishido stands firm in his position that Article 611 is a default provision that may be modified by the company's constitution.<sup>266</sup>

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261. See Tōkyō Chihō Saibansho [Tokyo Dist. Ct.] Apr. 27, 1995, 1541 HANREI JIHŌ 130 (Japan) (weighting DCF and net asset value 6:4).

262. Shishido, *Valuation*, *supra* note 229, at 428 n.3. Indeed, in its 1969 judgment the Supreme Court held that the lower court did not err in valuing the land at issue on a market value basis rather than book value. Saikō Saibansho [Sup. Ct.] Dec. 11, 1969, 23(12) MINSHŪ 2447, at 2, [https://www.courts.go.jp/app/files/hanrei\\_jp/974/051974\\_hanrei.pdf](https://www.courts.go.jp/app/files/hanrei_jp/974/051974_hanrei.pdf) (last visited Sept. 15, 2020) [<https://perma.cc/U359-CKFS>] (archived July 13, 2020) (Japan) (cited pagination only in online version of case).

263. RONTEN KAISETSU, *supra* note 239, at 563.

264. *Id.* at 590.

265. Egashira, Ōsugi, Niinomi, Itō & Kuroda, *Panel Discussion*, *supra* note 227, at 18 (Statements by Egashira Kenjirō (expressing doubt), Ōsugi Ken'ichi (arguing that Article 611, Paragraph 2 is a default rule but conceding the plausibility of an alternative interpretation), and Niinomi Hiroshi (acknowledging the possibility that the provision is a mandatory one and also hinting at tax implications)).

266. Shishido, *GK Joint Ventures*, *supra* note 225, at 238 n.54 (arguing that an interpretation of Article 611 as a mandatory rule would be at odds with the general legislative intent to reserve to the parties the broadest possible contractual freedom).

Amidst this uncertainty and the absence of any definitive case precedent, it seems at least arguable, if not implicitly conceded, that the company may specify a valuation mechanism in its constitution. From a practical standpoint, the important questions are whether there are limits to the company's freedom to do so and the content of those limits, if any. A strand of pre-*Kaisha-hō* doctrine suggests that the company's discretion is unfettered in this respect, and even a constitutional provision specifying that an exited member should receive no refund would be enforceable.<sup>267</sup> Countering this is another doctrinal strand arguing that extreme provisions in a corporate constitution, such as those denying outright or severely restricting the exiting member's refund, may be at odds with the fundamental for-profit nature of the membership company.<sup>268</sup> In particular, constitutional provisions denying refunds outright may be invalid.<sup>269</sup>

#### VI. THE FUTURE: THE TRAJECTORY OF WITHDRAWAL JURISPRUDENCE AND SCHOLARSHIP IN JAPAN

##### A. *The GK's Growing Popularity and Legal Significance*

Going forward, withdrawal's importance to Japanese corporate law appears to be entirely dependent on the GK's popularity as a corporate form. The critical question is: What are the GK's prospects?

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267. Matsumoto, *supra* note 249, at 264.

268. *Id.* at 265.

269. Ōsugi Ken'ichi, *Mochibun Kaisha, Minpō Kumiai no Hōritsu Mondai* [*Legal Issues in Membership Companies and Civil Law Partnerships*], in KAISHA, KIN'YŪ, HŌ (JŌ-KAN) [CORPORATIONS, FINANCE, LAW (VOL 1 OF 2)] 53, 79 (Iwahara Shinsaku, Yamashita Tomonobu & Kanda Hideki eds., Shōjihōmu 2013).

The GK has not lived up to the expectations surrounding its birth. Subject to corporation tax and denied the pass-through tax advantages that were a key motivation behind the GK's US LLC-inspired design, the greatest merit of the new form as originally conceived was lost.<sup>270</sup> Ten years on, the GK remains something of a novelty to the Japanese people<sup>271</sup> and is at a disadvantage in terms of brand name recognition compared to the KK.<sup>272</sup> Website articles by legal, accounting, and tax professionals targeted at people interested in incorporating companies point out differences between the KK and GK that might seem banal to the uninitiated outsider, but which are of a practical nature and carry weight in the Japanese business context. Take, for example, the titles that may be used by business owners on their business cards. Those who prize the time-honored and universally recognized "representative director" (*daihyō torishimariyaku*) title have no choice but to use a KK, whereas those who would be satisfied with "representative member" (*daihyō sha'in*) may find the GK adequate.<sup>273</sup> However, as the Japanese word for member (*sha'in*) in the nonlegal context nearly always means an "employee" of a firm,<sup>274</sup> representative members run the risk of being mistaken as mere company employees due to a linguistic quirk. The perceived gap in status between the "high-ranking" KK-representative director and the "mere employee" GK-representative member should not be underestimated in Japan's status-conscious society. However, there are exceptions to the GK's branding weaknesses; the importance of choice of corporate form to the business' brand value varies by industry.<sup>275</sup>

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270. Sekiguchi & Nishigaki, *supra* note 162, 18–19.

271. See Setsuyaku Shachō Henshūbu [Thrifty CEO Editorial Board], *Kabushiki Kaisha wa mō Jidai Okure! Gōdō Kaisha ga Kyūzō suru Riyū to wa* [*The KK Is Already Behind the Times!? Reasons for the Rapid Increase in GKs*], SETSUYAKU SHACHŌ [THRIFTY CEO] (July 8, 2015), <https://web.archive.org/web/20190601164132/https://setsuyaku.ceo/post/505/> 株式会社はもう時代遅れ-合同会社が急増する理 [<https://perma.cc/6VHV-TNQ5>] (archived July 8, 2020) (“登記数は増加傾向にあるとはいっても「株式会社」と比べれば、合同会社はまだに世間の信用イメージが低い。特に法人との取引においてはなおさらである。[“Despite growth in registrations, as compared to the KK the GK still enjoys less trust from the public. This is especially so in transactions with corporates.”]).

272. Uchida Atsushi, *Hōjin-ka (Hōjin Nari) Suru nara Kabushiki Kaisha to Gōdō Kaisha wa Docchi ga Ii?* [*If I Were to Incorporate, Which Is Better – KK or GK?*], UCHIDA ATSUSHI ZEIRISHI JIMUSHO [OFFICES OF UCHIDA ATSUSHI, CERTIFIED PUBLIC TAX ACCOUNTANT], (Apr. 1, 2016), <https://web.archive.org/web/20171028160344/https://www.uchitax.com/2016/04/01/comp-an-y-formation-llc/> [<https://perma.cc/YR7A-VA6V>] (archived July 9, 2020).

273. See, e.g., *id.*; Subaru Juku Un'ei Kanri-nin [Operations Manager, Subaru School], *Gōdō Kaisha to Kabushiki Kaisha no Chigai wo Osaeru 14 no POINTO* [*The Differences Between the GK and the KK in 14 Points*], SUBARU JUKU [SUBARU SCHOOL], (May 27, 2015), <https://web.archive.org/web/20171028160612/http://subaru-juku.com/llc->

Despite obstacles and teething troubles, the tide appears to be turning in favor of the GK. Since the GK became available in 2006,<sup>276</sup> incorporation numbers have risen steadily, according to business registration records from the Ministry of Justice.<sup>277</sup> The figures with separate breakdowns for new incorporations and incorporations via mergers or entity conversions are as follows:

Table 1 *Growth of GKs 2006–2018*

Year	New Incorporations	Mergers & Conversions	Total <sup>1</sup>
2006 <sup>2</sup>	3,392	58	3,450
2007	6,076	110	6,186
2008	5,413	90	5,503
2009	5,771	109	5,880
2010	7,153	114	7,267
2011	9,130	115	9,245
2012	10,889	138	11,027
2013	14,581	144	14,725
2014	19,808	158	19,966
2015	22,223	158	22,381
2016	23,787	148	23,935
2017	27,270	160	27,430
2018	29,076	159	29,235

Source: *Business Registration Statistics, Ministry of Justice (as of 31 May 2019)*<sup>278</sup>

joint%E2%80%90stock-company-difference-867 [https://perma.cc/3MCN-2JZW] (archived July 9, 2020).

274. Cf. 社員, WEBLIO, <https://ejje.weblio.jp/content/%E7%A4%BE%E5%93%A1> (last visited Aug. 19, 2020) [https://perma.cc/BQ6F-W2DF] (archived July 9, 2020) (translating the Japanese word for “member” into English; one definition includes “employee (of a company)” and most derivative terms and examples given are based on this meaning).

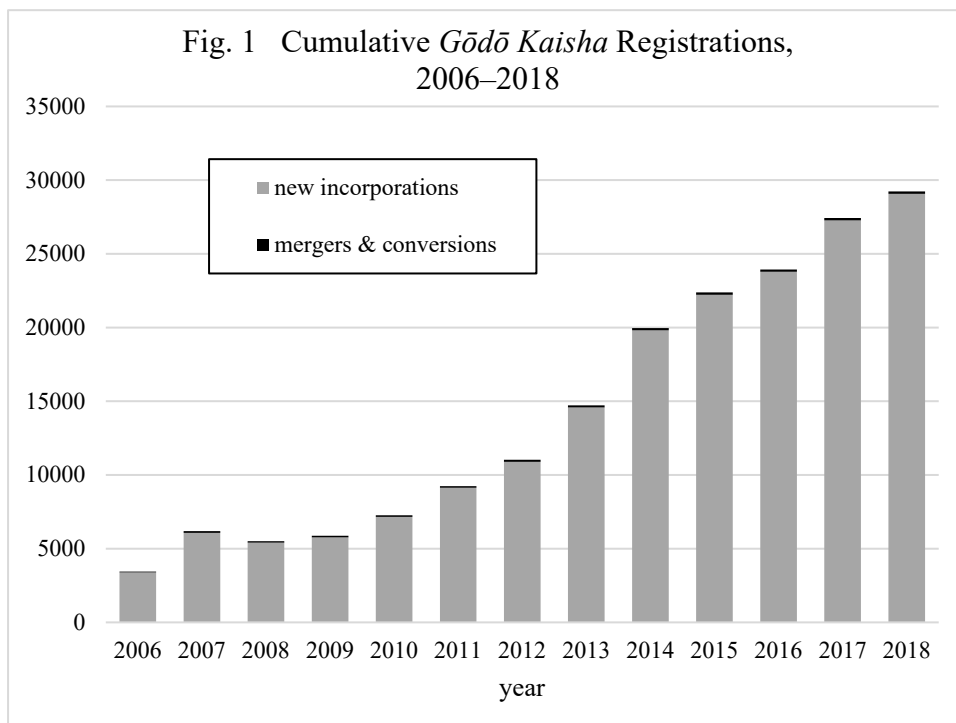
275. *Shiranai to son suru? Gōdō Kaisha no MERITTO, DEMERITTO [At a Disadvantage If You Don't Know? Pros and Cons of GKs]*, KEIEI HAKKĀ [MANAGEMENT HACKER], (Sept. 27, 2013), [https://web.archive.org/web/20171028160912/https://keiei.freee.co.jp/2013/09/27/goudou\\_gaisya/](https://web.archive.org/web/20171028160912/https://keiei.freee.co.jp/2013/09/27/goudou_gaisya/) [https://perma.cc/N5JP-YWSR] (archived July 9, 2020) (listing the respective merits of setting up GKs in the care, construction, food and beverage, aesthetics and beauty, property leasing, information technology (IT), consulting, and foreign exchange investment industries).

276. The Kaisha-hō entered force on May 1, 2006. *Kaisha Hō no Shikō Kijitsu wo Sadameru Seirei* [Cabinet Order Establishing the Effective Date of the Companies Act], Cabinet Order No. 77 of 2006, KANPŌ [OFFICIAL GAZETTE], Supp. No. 69, at 10.

277. See *infra* note 278.

278. SŌMU-SHŌ TŌKEI-KYOKU [STATISTICS BUREAU, MINISTRY OF INTERNAL AFFAIRS AND COMMUNICATIONS], *Shōgyō, Hōjin Tōki (Nenji-hyō) [Business and Corporation Registrations (Multiyear Statistics with Yearly Breakdowns)]*, E-STAT:





The doubling of new incorporations over the 2012–2015 period suggests that the GK might finally be coming into its own as a recognized, viable corporate form. By comparison, KK incorporations (new and by merger or entity conversion) never regained their post-*Kaisha-hō* peak at 114,928 in 2007; from 2009 to 2018 they have fluctuated between 85,000 and 95,000 each year.<sup>279</sup> Although the GK is likely to continue playing catch-up to the KK for the foreseeable future, the narrowing gap augurs well for the GK.

If GKs become an increasingly valued part of the economic landscape of the world's third-largest—and second-largest developed—economy, growth in their broader significance to Japanese and comparative corporate law will follow. This applies to withdrawal. Given the continuing proliferation of GK businesses, it is likely that

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PORTAL SITE OFFICIAL STATISTICS OF JAPAN, (May 31, 2019 & May 31, 2016), <https://www.e-stat.go.jp/stat-search/files?page=1&layout=datalist&toukei=00250002&tstat=000001012460&cycle=7&year=20180&tclass1=000001012462> (last visited Feb. 23, 2020) [<https://perma.cc/9APV-X339>] (archived July 30, 2020), <http://www.e-stat.go.jp/SG1/estat/List.do?lid=000001153179> (last visited Feb. 23, 2020) [<https://perma.cc/DGY9-3U2B>] (archived July 30, 2020) (focusing in particular on tables 18-00-16, 18-0018, 18-00-19, 18-00-20, 15-00-16, 15-00-18, 15-00-19, and 15-00-20). Incorporations by company splits, which range from 1 to 12 cases per year, *id.*, are not included in the figures in Table 1.

279. *Id.* (data found in tables 18-00-16 and 15-00-16).

incidents of members withdrawing will increase with time. The salience of the withdrawal regime to GKs will also grow correspondingly as more withdrawal cases will appear in court and in the law reports, providing valuable raw material for scholars and commentators to chew on. There is hope that attorneys and judges will devise less problematic legal solutions than in the past<sup>280</sup>—but where should they turn for guidance?

*B. Standing on the Shoulders of Giants: What the Law and Scholarship of the United States, United Kingdom, and Germany Can Contribute to the Development of Withdrawal in Japan*

More than ten years since the *Kaisha-hō* went into force, there is still hardly any jurisprudence on withdrawal from the GK. While this may be cause for concern for practitioners and businesses seeking certainty, there is also opportunity. In contrast to the KK (and YK), the GK has clear statutory language—in particular, “unavoidable grounds”—authorizing withdrawal.<sup>281</sup> The absence of firm judicial precedent constraining the scope of withdrawal also means that there is still a possibility of developing an effective withdrawal remedy catering to the needs of close corporations in Japan. The primary difficulty, however, is with the state of the domestic debate in Japan. There is existing domestic Japanese scholarship on the GK drawing on the very limited body of literature inherited from legacy membership company forms and from the pre-*Kaisha-hō* era,<sup>282</sup> but that by itself is inadequate to meet the needs of a modern and increasingly popular close corporation form.

That is where comparative corporate law has much to offer. It is a fact that close corporations are a shared phenomenon in leading, developed economies; it is also true that withdrawal is a common feature in such jurisdictions.<sup>283</sup> Notwithstanding the fact that it would be highly unusual for Japanese practicing jurists (whether attorneys or judges) to draw directly on foreign scholarship and precedent in preparing legal opinions or deciding cases applying local (Japanese) corporate law, academic jurists are not so constrained. Even outside the realm of law reform, there is scope for scholars to enrich the legal

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280. See *supra* Part III.C.1 (discussing past approaches in Ks and YKs).

281. *Kaisha-hō*, art. 606(3).

282. This is especially true for the law on withdrawal. See, e.g., Shishido, *Introduction to Part III*, *supra* note 161, at 13–14.

283. See *supra* Part II.C (illustrating the prevalence of withdrawal remedies in leading economies); *infra* Part VI.B.1–3 (discussing the applicability of withdrawal remedy principles from leading economies to the development of the withdrawal remedy in Japan); see also Alan K. Koh, *Shareholder Protection in Close Corporations: Theory, Operation, and Application of Shareholder Withdrawal* (unpublished Dr. jur. dissertation, Goethe University Frankfurt, June 4, 2019) [hereinafter Koh, *Shareholder Protection*] (on file with the editors).

discourse by using comparative corporate law analysis of appropriate foreign laws when preparing expert opinions or writing scholarly commentary that would be read and relied upon by practicing jurists.

The goal of this Part is to get the hypothetical ball rolling on using comparative corporate law to strengthen discourse on the Japanese GK, whether in a purely domestic (Japanese) or comparative setting. It briefly touches on the law on withdrawal in three leading developed jurisdictions—the United States, the United Kingdom, and Germany—for insights that may benefit the development of GK’s withdrawal regime and then offers a brief assessment of potential lines of inquiry that jurists working on the GK may find worthwhile to explore.

### 1. United States: Greater Complexity without Corresponding Guidance

What little foreign influence there is in Japanese legal scholarship on withdrawal in the GK appears to be primarily American.<sup>284</sup> The most prominent key players in GK law—Shishido Zen’ichi and Ōsugi Ken’ichi, as well as Egashira Kenjirō, the intellectual force behind the *Kaisha-hō*—draw predominantly on US LLC law and literature to the exclusion of every other foreign law.<sup>285</sup> However, there is reason to maintain a healthy skepticism about exclusive or excessive reliance on US LLC law in discourse on the Japanese GK.

First, the basis for looking to the US LLC—or more precisely, the individual LLC forms of the more than fifty states and territories with LLC statutes—for inspiration with respect to the GK as it stands has not been convincingly articulated in the Japanese literature. It is difficult to characterize the GK as it exists under the *Kaisha-hō* as a legal transplant of the US LLC because the GK *de lege lata* does not offer pass-through tax treatment.<sup>286</sup> The GK is, at best, a domestic entity “inspired by” or “initially modeled on” the *American* LLC but which ultimately has much more in common with other *Japanese* business entities.

Second, and specifically on the subject of withdrawal, federal taxation rules have been the driving force behind the US LLC throughout its entire history within the United States itself. Great

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284. See *infra* note 285 and accompanying text.

285. See, e.g., Egashira Kenjirō, *Gōdō-Kaisha Seido no MERITTO: Shimedashi Bōshi-saku no Sokumen* [The Merits of the GK Regime: The Aspect of Squeeze-out Prevention Measures], in MONGUCHI MASAHITO SAIBANKAN TAIKAN KINEN: ATARASHII JIDAI NO MINJI SHIHŌ [FESTSCHRIFT IN CELEBRATION OF JUDGE MONGUCHI MASAHITO’S RETIREMENT: CIVIL JUSTICE IN A NEW AGE] 241 (Matsushima Hideki, Itō Makoto & Fukuda Takahisa eds., Shōjihōmu 2011) (citing only US sources for foreign law except one tangential reference to a Japanese source on a point of German law not relevant to GKs or membership companies as such); Shishido, *Valuation*, *supra* note 229; Shishido, *Introduction to Part III*, *supra* note 230 (citing only US law); Ōsugi, *supra* note 225, at 212 n.12 (mentioning the UK LLP only once and tangentially).

286. See *supra* notes 161–162 and accompanying text.

demand existed for an entity that would qualify for partnership taxation without sacrificing limited liability. Prior to 1997,<sup>287</sup> the only way to do that was to ensure that the entity lacked at least two of the following three corporate characteristics: continuity of life, free transferability of interests, and centralization of management;<sup>288</sup> usually the first two.<sup>289</sup> The generous rights of withdrawal *at will* offered by the earliest state LLC statutes—which were often bundled with dissolution of the entity upon withdrawal of any member<sup>290</sup>—were designed to avoid a finding of continuity of life.<sup>291</sup> Once the Internal Revenue Service moved away from a corporate resemblance test and to a “check-the-box” regime where the entity can itself choose whether to be taxed as a corporation or partnership,<sup>292</sup> state legislatures gradually eliminated withdrawal.<sup>293</sup> Crucially, legislatures did not seem to have considered the implications of abolishing or curtailing withdrawal on member oppression (i.e., the close corporation problem).<sup>294</sup> The former prevalence of and subsequent disappearance of withdrawal from the LLC is thus driven by factors that do not hold even remotely true in Japan, where pass-through taxation is not permitted for the GK at all and there is only one uniform national-level statute for business corporate entities.

Although the United States’ experience with close corporations in the narrow sense (i.e., non-LLCs) avoids many of the problems with LLC law and jurisprudence, it is not without its own flaws. It is beyond

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287. When “check-the-box” regulations permitting the entity to elect whether to be taxed as a corporation or partnership went into force. See Simplification of Entity Classification Rules, 61 Fed. Reg. 66,584, 66,587 (Dec. 18, 1996) (providing that changes to 26 C.F.R. § 301.7701, among other provisions, would take effect January 1, 1997).

288. See Susan Pace Hamill, *The Taxation of Domestic Limited Liability Companies and Limited Partnerships: A Case for Eliminating the Partnership Classification Regulations*, 73 WASH. U. L.Q. 565, 573 (1995) (citing 26 C.F.R. § 301.7701-2 (as amended in 1993)).

289. Carter G. Bishop, *Treatment of Members Upon Their Death and Withdrawal from a Limited Liability Company: The Case for a Uniform Paradigm*, 25 STETSON L. REV. 255, 259–60 & n.17 (1995); Moll, *Minority Oppression*, *supra* note 51, at 929–30.

290. Dissolution could be avoided, but the withdrawing member would be entitled to have their interest bought out. Moll, *Minority Oppression*, *supra* note 51, at 928.

291. *Id.* at 930.

292. 26 C.F.R. §§ 301.7701-1–301.7701-3 (2020) (defining and classifying business entities for tax purposes); for the Internal Revenue Service’s evolving approach to LLC taxation and role in the drafting of LLC statutes, see Susan Pace Hamill, *The Origins Behind the Limited Liability Company*, 59 OHIO ST. L.J. 1459, 1466–84 (1998).

293. Moll, *Minority Oppression*, *supra* note 51, at 932–40. Compare ULLCA 1996 §§ 601(1) (providing for a default right to withdraw at will), 701(a)(1) (providing for a default obligation of LLC to buy out the withdrawing member’s interest) with Uniform Limited Liability Company Act §§ 601(a) (providing for default power to dissociate at will), 603(a)(3) and 404(b) and comments thereto (no provision for a default right of dissociating member to receive a distribution for their interest) (UNIF. LAW COMM’N 2013). On modern “Hotel California” provisions, see ROBERT R. KEATINGE, LARRY E. RIBSTEIN & THOMAS E. RUTLEDGE, RIBSTEIN AND KEATINGE ON LIMITED LIABILITY COMPANIES § 14:2 & n.4 (2d ed. 2010) (loose-leaf).

294. See Moll, *Judicial Dissolution*, *supra* note 52, at 106–07.

reasonable doubt that the law and jurisprudence of close corporations in the United States is diverse and complex.<sup>295</sup> Complicating matters is the fact that Delaware, notwithstanding its dominance in the publicly listed corporation sphere, is not a dominant player in the close corporation universe,<sup>296</sup> and is particularly hostile to withdrawal.<sup>297</sup> It is neither desirable nor practical for Japanese jurists to devote vast amounts of attention and energy to a rigorous study of US close corporations in their full variety spread across more than fifty states and territories. US close corporation law thus offers little in the way of clarity or convenience to foreign jurists seeking to understand it for practical, law reform-oriented purposes.

This Article's assessment that US law is not an appropriate subject for comparison may surprise, given the fact that, for better or worse, the United States (often Delaware specifically) is widely used as a comparator jurisdiction in comparative corporate law both in and out of Japan.<sup>298</sup> Fortunately, there are other similarly advanced economies with sophisticated legal systems that have developed relatively coherent and sophisticated bodies of jurisprudence on withdrawal that deserve greater attention as subjects of comparative corporate law. Next up for a closer look are two such jurisdictions: the United Kingdom and Germany.

## 2. United Kingdom: Proven Track Record of Shareholder Protection against Economically Harmful Conduct through Unfair Prejudice

At first glance, the United Kingdom may be a relatively odd choice of comparator jurisdiction with Japan, given that the two nations'

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295. For leading treatises, see generally DOUGLAS K. MOLL & ROBERT A. RAGAZZO, *CLOSELY HELD CORPORATIONS* (2017); O'NEAL AND THOMPSON'S OPPRESSION OF MINORITY SHAREHOLDERS, *supra* note 2; O'NEAL AND THOMPSON'S CLOSE CORPORATIONS AND LLCs, *supra* note 18.

296. See generally Jens Dammann & Matthias Schündeln, *The Incorporation Choices of Privately Held Corporations*, 27 J.L. ECON. & ORG. 79 (2009) (reporting that most closely-held corporations in the US incorporate in the state where the corporation has its primary place of business).

297. See *Nixon v. Blackwell*, 626 A.2d 1366, 1380–81 (Del. 1993) (rejecting the notion that the court has the power to order buyouts in the absence of express contractual arrangement).

298. See, e.g., Alan K. Koh, Masafumi Nakahigashi & Dan W. Puchniak, *Land of the Falling "Poison" Pill: Understanding Defensive Measures in Japan on Their Own Terms*, 41 U. PA. J. INT'L L. 687, 714–19 (2020) (comparing Japan and Delaware); KRAAKMAN, ARMOUR, DAVIES, ENRIQUES, HANSMANN, HERTIG, HOPT, KANDA & ROCK, *supra* note 13 (comparing the United States—and particularly Delaware—with other jurisdictions including Japan, the United Kingdom, Germany, France, Italy, and Brazil); Curtis J. Milhaupt, *In the Shadow of Delaware? The Rise of Hostile Takeovers in Japan*, 105 COLUM. L. REV. 2171, 2198–215 (2005) (comparing Japan and Delaware); Koh, *supra* note 85 (comparing Japan and Delaware); Shishido, *Introduction to Part III*, *supra* note 161, at 15 (citing California and Delaware statutes and a Uniform Act in the very paragraph discussing Article 606, Paragraph 3 of the Kaisha-hō); Shishido, *Incentive Bargaining*, *supra* note 230 (comparing Japan and Delaware).

corporate laws have little connection by way of direct transplant or transfer,<sup>299</sup> and that scholars working on UK law—or even Anglo-Commonwealth law more broadly—are a relative minority in Japanese legal academia.<sup>300</sup> The United Kingdom's domestic corporate law is particularly useful when it comes to the subject of withdrawal—which takes the form of share buyout orders made under the court's unfair prejudice jurisdiction—for two reasons.

First, unfair prejudice is a popular, proven remedy with a substantial body of legal writing. In particular, extensive practitioner treatises<sup>301</sup> summarizing salient points of the United Kingdom's burgeoning body of relatively uniform unfair prejudice jurisprudence make it relatively accessible even to foreign audiences.

Second, the courts have taken to making judicial adjustments when performing share valuations that take into account actions and behavior of the defendant that have had the effect of decreasing corporate value or specific detriment to the plaintiff shareholder.<sup>302</sup> This has the effect of achieving fairer results in individual cases and strengthening the extent of the protection conferred by the unfair

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299. An oft-cited example of UK influence on Japanese corporate and securities law is the mandatory bid rule; however, not only is that not strictly speaking binding “corporate law,” but the characterization of the Japanese mandatory bid rule as modeled on the UK is questionable at best. See Dan W. Puchniak & Masafumi Nakahigashi, *The Enigma of Hostile Takeovers in Japan: Bidder Beware*, 15 BERKELEY BUS. L.J. 4, 6 n.4, 24–27 (2018) (distinguishing the Japanese regime from that of the United Kingdom). More recently, the UK has exerted great influence via its Stewardship Code, although the resulting Japanese product differs from the UK original in material respects. Compare Gen Goto, *The Logic and Limits of Stewardship Codes: The Case of Japan*, 15 BERKELEY BUS. L.J. 365, 383 (“The framework of the Japanese Stewardship Code is heavily influenced by the UK Stewardship Code.”) with Gen Goto, Alan K. Koh & Dan W. Puchniak, *Diversity of Shareholder Stewardship in Asia: Faux Convergence*, 53 VAND. J. TRANSNAT'L L. 829, 872–74 (2020) (analyzing the differences between Japan's stewardship code and the codes of the UK and Singapore).

300. On withdrawal specifically, see generally HIROTA TETSUJI, SHŌSŪ KABUNUSHI NO HOGO TO KYŪSAI [MINORITY SHAREHOLDER PROTECTION AND REMEDIES] (Dai'ichihōki 2013) (comparing Japan with the UK and Canada); SAKAMAKI, *supra* note 73 (comparing Japan with the UK and US); Kawashima Izumi, *Shōsū Kabunushi ni taisuru Fukōsei Shingai Kōi-tō no Kyūsei Seido (1)* [*The Regime for Relief of Unfairly Prejudicial Conduct Towards Minority Shareholders (1)*], 98 MINSHŌHŌ ZASSHI 535 (1988) (examining the UK and Canada).

301. Useful treatises include ROBIN HOLLINGTON, HOLLINGTON ON SHAREHOLDERS' RIGHTS ch. 7 (8th ed., Sweet & Maxwell 2017) (discussing the unfair prejudice remedy) and Victor Joffe & Timothy Collingwood, *Unfair Prejudice: The Statutory Remedy*, in MINORITY SHAREHOLDERS: LAW, PRACTICE AND PROCEDURE ch. 6 (Victor Joffe, David Drake, Giles Richardson, Daniel Lightman & Timothy Collingwood eds., 6th ed. Oxford University Press 2018) (same).

302. See, e.g., *Maidment v. Attwood* [2012] EWCA (Civ) 998, [2013] 2 BCLC 567 [26] (Eng.) (Arden, LJ) (“[A]ctual share values can be adjusted [by the court] to reflect the effect on the company of all or any wrongs which the wrongdoer respondents have committed against it”); see also Alan K. Koh, *Reconstructing the Reflective Loss Principle*, 16 J. CORP. L. STUD. 373, 387–89 (2016) [hereinafter Koh, *Reflective Loss Principle*] (noting that courts have taken unfairly prejudicial conduct into account when valuing a petitioner's shares).

prejudice remedy.<sup>303</sup> As it stands, there is arguably room within the applicable statutory language of Japan's *Kaisha-hō* to implement a similar system of judicial adjustment.<sup>304</sup>

Third, the usual relief ordered under the unfair prejudice jurisdiction—an order that the “wrongdoer” member (defendant) purchase the shares of the aggrieved withdrawing member (plaintiff)—has a particular strength: it does not involve any financial outlay by the company.<sup>305</sup> A buyout order targeted at a wrongdoing member may thus be ordered by the court and on generous valuation terms (including possible judicial adjustment as discussed above) without threatening the company as a going concern.<sup>306</sup> A potential objection to implementing a UK-style buyout order may be that there is no clear statutory language in Japan's *Kaisha-hō* authorizing the court to compel any member of a GK (instead of the GK itself) to pay for the withdrawing member's membership interest. Nevertheless, there is again opportunity in legislative silence; in the absence of clear statutory language *prohibiting* a court order to pay compensation to be directed at a wrongdoing co-member, it is still possible to develop a

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303. See Koh, *Reflective Loss Principle*, *supra* note 302, at 387–89 (illustrating how accounting for defendants' actions can affect the outcomes of cases involving claims of unfair prejudice); see also Koh, Shareholder Protection, *supra* note 283, at ch. III.G.3.ii (pp. 103–04) (noting, in the context of the UK [and to a lesser extent, the US] that “[n]ot only would the withdrawing shareholder as a starting point reclaim the value of their membership interest, they also stand a chance of being compensated for their “share” of the loss caused to the close corporation by the party responsible for the grounds of withdrawal ... The Anglo-American approach is more targeted by requiring clear attribution of fault, but also more powerful from the perspective of minority protection. It serves a compensatory function as the party at fault is liable to make the victim whole again.”).

304. See *Kaisha-hō*, [Companies Act], Law No. 86 of 2005, art. 611(2) (Japan) (“Accounting as between the member who has exited and the membership company shall be conducted on the basis of the company's asset situation as at the time of exit.”). If the wrongdoing party's conduct is also separately actionable by the company under corporate law or the general law of obligations (contract, tort, or unjust enrichment), it may well be possible to take those potential claims into account when assessing the company's “asset situation.” Implementing a system of judicial adjustments similar to that of the UK in the context of a regime where the company (the GK) is required to pay compensation to the withdrawing member may theoretically impose a greater burden on the GK. However, this would be alleviated in whole or part by additional incentive for the GK to recover the value of the additional payout to the withdrawing member by pursuing claims against wrongdoing members.

305. The “usual relief” is a share buyout order. See *supra* notes 57–58 and accompanying text; see also Koh, Shareholder Protection, *supra* note 283, at ch. III.G.3.ii (p. 103) (“With the close corporation not usually on the hook, business creditors' interests are not affected as a matter of corporate law, and thus pose no obstacle to the withdrawing shareholder's ability to enforce their monetary claim.”).

306. Cf. Aizawa & Kōriya, *supra* note 184, at 165 (noting that the withdrawn member has no choice but to apply for dissolution of the GK and receive a distribution upon liquidation if the GK's executive member(s) fails to take the necessary steps to pay the refund). A further benefit of imposing the burden of paying compensation on a member rather than the GK itself is that any concerns with prejudice to creditors would be alleviated.

version of this through decisive judicial action. As it turns out, there is one jurisdiction—a *civil law* jurisdiction, in fact—that developed its withdrawal regime for its leading close corporation entity entirely without any basis in the statutory text: Germany.<sup>307</sup>

### 3. Germany: Versatile, Judicially Developed Relief for a Wide Range of Situations

Germany might seem an unlikely candidate for comparative study, especially since Japan made a deliberate decision to get rid of the YK<sup>308</sup>—a close corporation form descended<sup>309</sup> from the German GmbH. Nevertheless, the German variant of withdrawal—*Austritt aus wichtigem Grund*—is valuable as it offers a model for the development of unavoidable grounds in the context of withdrawal from the GK.

Never codified into GmbH legislation,<sup>310</sup> withdrawal in Germany is based on the core concept of “*wichtiger Grund*.” This is a settled doctrine whereby a GmbH member has the right to withdraw when a *wichtiger Grund*—“important reason” or “good cause”—is established; this *wichtiger Grund* can be anything that makes it unbearable (*unzumutbar*) for the member to remain in the GmbH.<sup>311</sup> Whether a *wichtiger Grund* would be recognized in any particular case would turn on an overall assessment (*Gesamtabwägung*) of the respective circumstances and interests of the parties involved,<sup>312</sup> making it a

307. See *infra* note 310 and accompanying text.

308. See *supra* Part III.A; see also *supra* notes 79–80 and accompanying text (discussing the repeal of the YK Act).

309. See *supra* note 73 and accompanying text (describing the influences contributing to the YK Act).

310. GOETTE, *supra* note 35, at 97.

311. Bundesgerichtshof [Federal Court of Justice] Dec. 16, 1991, ENTSCHEIDUNGEN DES BUNDESGERICHTSHOFES IN ZIVILSACHEN [BGHZ] 116, 359, 369 (Ger.); Peter Ulmer & Mathias Habersack, *Anhang § 34 Ausschließung und Austritt von Gesellschaftern* [Appendix to Section 34: Expulsion and Withdrawal of Members], in GESETZ BETREFFEND DIE GESELLSCHAFTEN MIT BESCHRÄNKTER HAFTUNG (GMBHG): GROßKOMMENTAR [LAW ON LIMITED LIABILITY CORPORATIONS: GRAND COMMENTARY] Rn 51 (Peter Ulmer, Mathias Habersack & Marc Löbbe eds., 2d ed., Mohr Siebeck 2014). An alternative way of phrasing the test is “*unreasonable to expect or require* the member to remain in the GmbH.”

312. GERHARD K. BALZ, DIE BEENDIGUNG DER MITGLIEDSCHAFT IN DER GMBH: EINE EMPIRISCHE UND DOGMATISCHE UNTERSUCHUNG ZUR AUSSCHLIEßUNG UND ZUM AUSTRITT VON GESELLSCHAFTERN [THE TERMINATION OF MEMBERSHIP IN THE GMBH: AN EMPIRICAL AND DOCTRINAL STUDY OF EXPULSION AND WITHDRAWAL OF MEMBERS] 106–07 (Duncker & Humblot 1984) (providing examples); HANS-FRIEDRICH MÜLLER, DAS AUSTRITTSRECHT DES GMBH-GESELLSCHAFTERS [THE GMBH-MEMBER'S WITHDRAWAL RIGHT] 52 (Carl Heymanns 1996); Lorenz Fastrich, *Anhang nach § 34 Ausschluss und Austritt von Gesellschaftern* [Appendix to Section 34: Expulsion and Withdrawal of Members], in GMBHG: GESETZ BETREFFEND DIE GESELLSCHAFTEN MIT BESCHRÄNKTER HAFTUNG [GMBH LAW] Rn 19–20 (Adolf Baumbach & Alfred Hueck eds., 20th ed., C.H.



powerful yet flexible concept applicable to a wide range of circumstances. In this regard, *wichtiger Grund* and unavoidable grounds are similarly open-textured—and thus versatile—concepts.

Despite the considerable merits of drawing on German doctrine and scholarship on withdrawal, it is not without its own obstacles. Although Japan retains, in part, the academic tradition of taking German corporate law and scholarship seriously, overall German influence on Japanese corporate law scholarship appears to be waning.<sup>313</sup> As Takahashi observes, there has been for some years little direct exchange of ideas between Japanese and German corporate law.<sup>314</sup> In the GK context, with the memory of US LLC influence on the GK as it was originally conceived but not ultimately enacted, as well as the abolishment of the German GmbH-inspired YK, it may be unsurprising that the German law-inspired legal scholarship in this field has been eclipsed by its US-inspired counterpart—especially among the generation of scholars still actively writing.<sup>315</sup> This is unfortunate: with no significant body of new cases under the *Kaisha-hō* regime immediately at hand, it is more important than ever for scholars and commentators to draw on foreign law for inspiration and insight. Yet, those sources are growing increasingly impoverished; notwithstanding the efforts of a vocal minority in keeping German corporate law scholarship alive in Japan, the wealth of experience and knowledge on the GmbH may very well in time be forgotten.

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Beck 2013) (providing examples); Christoph H. Seibt, *Anhang § 34: Austritt und Ausschließung eines Gesellschafters* [Appendix to Section 34: Withdrawal and Expulsion of a Member], in I KOMMENTAR ZUM GMBH-GESETZ [COMMENTARY ON THE GMBH LAW] Rn 10–13 (Franz Scholz ed., 11th ed., Dr. Otto Schmidt 2012) (providing examples); Lutz Strohn, § 34 *Einziehung von Geschäftsanteilen* [Section 34 Redemption of Membership Interests], in I MÜNCHENER KOMMENTAR ZUM GESETZ BETREFFEND DIE GESELLSCHAFTEN MIT BESCHRÄNKTER HAFTUNG – GMBHG [MUNICH COMMENTARY ON THE LAW ON LIMITED LIABILITY CORPORATIONS] Rn 180 (Holger Fleischer & Wulf Goette eds., 3d ed., C.H. Beck 2018).

313. Takahashi Eiji is one of the few scholars who continue to draw inspiration from German law when writing on the GK. See, e.g., Eiji Takahashi, “Reception” and “Convergence” of Japanese and German Corporate Law, 12 U. ST. THOMAS L.J. 228, 240–47 (2015) [hereinafter Takahashi, “Reception” and “Convergence”] (detailing the ways German and Japanese corporate law have “grown more similar without mutual exchange”); see also Masuda Masaaki & Urakawa Shōji, *Gōdō-Kaisha kara no Sha’in no Taisha ni kansuru Shomondai* [Issues in Member Withdrawal from the GK], 58-2/3 KINKI DAIGAKU HŌGAKU 99 (2010).

314. Takahashi, “Reception” and “Convergence,” *supra* note 313, at 240–47 (observing that Japanese and German corporate law are “converging” in terms of substantive content due to influence from US law); see also TAKAHASHI EIJI, KAISHA HŌ NO KEIJU TO SHŪREN [RECEPTION AND CONVERGENCE OF CORPORATE LAW] (Yūhikaku 2016).

315. See *supra* note 285 and accompanying text (listing a variety of sources from leading scholars).

## VII. CONCLUSION

Solutions and insights can come from unexpected places; such is the case in Japan for close corporation law, the corporate law of the ordinary (business) people. The lack of withdrawal in Japan's close corporation forms pre-2005 drew responses that created further problems. Despite general consensus on the importance of formal withdrawal remedies and support from the scholarly community, direct legislative reform efforts in the 1980s went nowhere. Yet, withdrawal has ultimately entered contemporary Japanese corporate law, if almost as an afterthought, as part of the new GK. In turn, the GK is now the only viable Japanese close corporation form with limited liability for all members offering a member's withdrawal regime.

This new GK withdrawal regime—centered on the open-ended concept of “unavoidable grounds”—offers members of GKs—and courts—the possibility of addressing and solving a wide range of shareholder conflicts with a single, targeted, and powerful remedy. It is not without its problems, especially when it comes to the withdrawn member's ability to enforce their entitlement to the refund of their membership interest. Driven primarily by advocates and specialists in joint venture law, contemporary discourse on the withdrawal regime, whether on the scope of “unavoidable grounds” or on valuation standards, is dominated by the debate on whether the *Kaisha-hō* provisions are default or mandatory rules, and, if default, the extent to which they may be modified by the corporate constitution. Little is settled at present with only limited jurisprudence of considerable vintage and not a single post-*Kaisha-hō* judicial precedent apropos the GK. The lack of attention devoted to the use of GKs and the withdrawal regime in non-joint venture contexts further hampers understanding and development of the law.

The extent to which the GK's popularity and importance would be impeded by the current legal uncertainty is an open question, although recent growth trends suggest the presence of significant and growing enthusiasm for the GK form notwithstanding the difficulties. Close corporation law in Japan is now at a crossroads; for the first time in Japanese legal history, participants in closely held businesses may enjoy both limited liability and possible access to the last and best hope of a minority participant in unacceptable circumstances—withdrawal. It is true that the KK remains a popular choice for new businesses relative to the GK, despite the absence of withdrawal in the former. This does not diminish in any way the importance of the system of withdrawal in close corporation law, as the reasons for choosing KKs have less to do with its intrinsic legal merits or suitability and more to do with historical familiarity, reputational advantages, and emotional

considerations.<sup>316</sup> The dearth of serious legal writing on the GK and the corresponding lack of awareness among legal practitioners of the GK's merits are also further obstacles to greater adoption of the GK as a business vehicle. The fact that GK formations are closing the gap with the KK despite the absence of a single overwhelming force (such as federal tax in the US LLC) suggests that, going forward, the KK's traditional advantages may no longer be sufficient to overcome the bundle of features offered by the GK—including withdrawal. It remains to be seen whether Japanese business owners would realize—and capitalize upon—the relative merits offered by the GK with its withdrawal remedy when choosing how to incorporate, and whether their legal advisors would recommend the use of withdrawal to obtain reasonably fair outcomes in situations of intractable shareholder conflict.

With the law of withdrawal yet to commit itself firmly to any direction, jurists hold in their grasp a historic opportunity to shape the future of close corporation law. There is no better time to deploy comparative corporate law in forging a path ahead for Japanese law, and there is no better way than for Japan's jurists to first wean themselves of their fascination with the messy ambivalence that is the US law on withdrawal in close corporations and LLCs. After all, no quantity, no matter how high the quality, of scholarship drawing exclusively on the United States, if any foreign jurisdiction at all, can overcome the limitations inherent in the monoculture of scholarly ideas. It is time for mainstream Japanese discourse and the comparative corporate law community at the international level to seek out other illuminating guiding lights; this Article has shown that one needs to look no further than the United Kingdom and Germany for places to start.

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316. *See supra* Part III.C.3 and Part VI.A (discussing and highlighting the differences between Japanese corporate forms and their respective characteristics).