

# Framework for New Growth Market

July 29, 2008

## 1. Purpose of the new market

An examination of the current capital raising environment for growing Japanese and Asian companies reveals a major gap that is not being met in existing Japanese or Asian markets.

Japanese companies : Japan's economy includes a class of companies that have solid business models and a strong need for risk capital, the needs of which have not been met by existing markets. In addition, the existing markets are not necessarily markets in which investment is made based on an assessment of enterprise value from a medium to long-term perspective, and even if a company successfully conducts an IPO, it may subsequently have difficulty procuring funds through secondary and subsequent offerings in line with its growth stage.

Asian companies : Asia is experiencing remarkable economic development and has many companies with strong needs to procure financing in the form of risk equity capital. Many of these companies have operational connections with Japan (Japanese customers, business partners, technology providers, etc.) or have received funding from Japan, and have a strong desire to attract Japanese investors and capital. Other Asian securities markets have not been able to fully meet the needs of these companies.

Tokyo Stock Exchange Group ("TSE") and London Stock Exchange Group ("LSE") believe that this funding gap can be reduced by the creation of a new market. As a result, major business opportunities are expected to emerge for issuers, investors, securities companies, legal specialists, accounting specialists and other stakeholders. This new market will generate revenues for all these businesses and contribute to the further economic development of Japan and Asia.

## 2. Creation of a new exchange

The two exchanges will establish a joint venture to operate the new market under a new exchange, which will be domiciled in Japan.

The new market will operate within the new legal framework introduced in Japan, pursuant to the Amendment law of the Financial Instruments and Exchange Act, as a market for professionals. The new market will be based on the AIM regulatory framework and Nomad system, tailored where appropriate to suit the needs of the Japanese and Asian markets, as described further in Appendix 1. The two exchange groups firmly believe that through this new market they can attract Japanese and Asian companies and international investors.

TSE will bring to the new market its expertise and capabilities in operating markets in Japan and Asia, while LSE will bring its expertise and capabilities in operating growth markets, gained from its operation of AIM, the most successful growth market in the world.

### **3. Legal Framework**

#### **(a) Background to the creation of the new legal framework**

- Under the existing law, the legal framework for stock markets does not make distinctions by type of investors, and the direct participation of retail investors is possible. The only exceptions to this are the rules relating to private placements, which only allow the distribution of stock to accredited institutional investors, similar to the 144A market in the U.S. Consequently, Japan's markets (including TSE Mothers), are subject to regulatory systems based on strong requirements for retail investor protection. These requirements have in recent times become more pronounced (internal controls reporting has been in force from April 2008 and quarterly disclosure is now mandatory).
- This position contrasts with a number of other countries, where highly flexible markets are being developed targeting particularly professional investors. Japan also recognizes a strong need to develop a market that distinguishes between professional investors and retail investors. Therefore, at the end of 2007, the First Subcommittee of the Sectional Committee on the Financial System of the Financial System Council recommended the development of a framework for a professionals-only market.
- The Financial Services Agency ("FSA") included this recommendation in its Plan for Strengthening the Competitiveness of Japan's

Financial and Capital Markets and the Amendment Law of the Financial Instruments and Exchange Act, which is based on the plan, was passed in June 2008 and is expected to be in force by the end of the year.

**(b) Key features of the legal framework**

- A new disclosure regime (for both admission and ongoing disclosure) will be adopted for securities listed on the new market, and such securities will only be available for distribution to “specified investors”, as defined below:
  - Accredited institutional investors
  - Listed companies
  - Joint-stock corporations with capital of ¥500 million or more
  - Other approved corporations\*
  - Approved individuals with net assets and financial assets of ¥300 million or more, and one year or more of trading experience\*  
(\*N.B. Any such corporation or individual would need to apply for and receive prior approval)
  
- Under this new principles-based regulatory regime, the format and language of listing information, corporate disclosures, accounting standards, and other requirements will not be prescribed in law. Furthermore, submission of disclosure documents to the FSA, the financial authority, will not be required
  
- However, to preserve market integrity, with regard to matters such as fraudulent disclosure, regulation of insider trading, the reporting of substantial shareholdings and takeover requirements, regulations and systems will apply as with existing listed securities

**4. Reference materials**

Further detail is set out in the following:

- The J-Nomad System and System for Listing on New Market are outlined in Appendix 1

- The trading system and the clearing and settlement system are outlined in Appendix 2
- The system for trading participants is outlined in Appendix 3

#### **5. Schedule for commencement of new market**

The Amendment Law of the Financial Instruments and Exchange Act, is scheduled to be enforced within six months of being passed on June 13, 2008, meaning that it should be effective by December 12, 2008 at the latest. The new exchange will promptly apply for authorization after the Amendment Law of the Financial Instruments and Exchange Act is enforced and, subject to the receipt of regulatory approval, will then commence operations.

Comments on this outline are welcomed from all market participants and should be sent to <http://www.tse.or.jp/english/rules/newmarket/index.html> by August 29th 2008.