THE 1988 JAPANESE INSIDER TRADING AMENDMENTS: WILL JAPAN SEE RESULTS FROM THESE TOUGHER LAWS?

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1. INTRODUCTION

From the visitor’s gallery, the Tokyo Stock Exchange, the world’s largest stock market, appears nearly identical to its United States counterpart in New York. It is, however, profoundly different at heart. Japan has been called an “insider’s heaven”; until recently insider trading has been a way of life. Although Japan’s markets are not unique in this respect, as insider trading is quite prevalent internationally, the impact upon other markets is significant due to the enormous size and power of the Tokyo Exchange.

For reasons discussed later in this Comment, the 1988 amendments to Japan’s Securities and Exchange Law (“SEL”) radically reformed Japanese laws governing insider trading. This Comment will


4 Insider trading is defined as the use of material, non-public information by those in privileged positions for their own personal gain. See Note, Extraterritorial Enforcement of Rule 10(b)-5: Insider Trading in the International Equities Market, 12 SUFFOLK TRANSNAT’L L.J. 83, 86 (1988).

5 There are eight exchanges in Japan - Tokyo, which is the largest, Osaka, Nagoya, Kyoto, Hiroshima, Fukuoka, Niigata and Sapporo. See Note, supra note 3, at 1303 n.50.

6 For example, in Britain, stock prices of companies targeted for takeovers frequently rise sharply at least one month prior to the official public announcement of the transaction, although insider trading has been illegal in that country since 1980. “In West Germany, where insider trading is not only tolerated but a term for insider does not exist in the language, stock prices regularly rise before improved earnings reports.” Hong Kong’s stock market has been likened to the Dodge City of international securities markets, as insider trades there are a way of life, despite laws to the contrary. See Insider Trading Probes Having Global Domino Effect, Chicago Tribune, March 5, 1989, Business, at 13, col. 1.

7 See generally Securities and Exchange Law, Law No. 25 of 1948 (as amended in 1988), translated in K. OKAMURA & C. TAKESHITA, LAWS AND REGULATIONS RELATING TO INSIDER TRADING IN JAPAN (1989) [hereinafter SEL].
discuss these amendments, the events which led to them, their content, and probable impact. Before the new law can be analyzed, however, it is necessary to understand the old law, the reasons behind its ineffectiveness, and why the Japanese government has failed to enforce it fully. With this background, one can appreciate the extent to which the new law's success hinges on its successful confrontation with insider trading in the Japanese securities markets.

2. INSIDER TRADING LAWS PRIOR TO THE 1988 AMENDMENT

The pre-1988 laws which regulated insider trading, adopted during the Allied Occupation of Japan, were modeled after provisions of the United States' Securities Act of 1933 and the Securities Exchange Act of 1934. Though these laws were imposed by the Allied Forces, they remained in force long after their departure. Although the Securities and Exchange Law has been amended nearly twenty times since its inception, it until recently closely mirrored American law. The central provision of the original insider trading rules was SEL Article 58, a general anti-fraud provision prohibiting the use of any fraudulent device in conjunction with securities transactions. This provision is

All of the SEL articles cited in this comment are as they appear following the 1988 amendments. I have used the 1988 amended version as this text reflects current law, while still embodying the same basic meaning of the original language in the 1948 acts. Due to the recent enactment of these laws, the official English translation of these 1988 amendments has not yet been published. I have used a translation prepared in Japan by Kuzami Okamura, Esq. and Chieko Takeshita, Esq., and compiled by the Secondary Market Division of the Securities Bureau, Ministry of Finance. The translation was published by the Commercial Law Center, Inc. in Tokyo, and I believe that it reflects a very reliable interpretation of the law.


The 1988 Amendments have left these provisions largely undisturbed. Instead of rewriting the law, the amendments have simply added to existing laws governing insider trading.

"Indeed, several of the amendments have tracked post-1948 developments in American securities law." Banoff, The Regulation of Insider Trading in the United States, United Kingdom, and Japan, 9 MICH. Y.B. INT'L LEGAL STUD., 145, 163 (1988). Moreover, Banoff notes, the Japanese still continue to pay close attention to changes in American securities regulation. Id. at 164.

Article 58 provides: No person shall commit any act set forth in the following Items:

(1) employ any device, scheme or artifice to defraud in connection with the purchase or sale of, or any other transaction with respect to, any security, or trading in securities index futures and similar tradings, trading in securities options and similar tradings, or trading in foreign market securities futures and similar tradings;

(2) obtain cash or other property by using a document or any other representation which includes any false statement with respect to a material
strikingly similar to Rule 10b-5 promulgated under the Securities Exchange Act of 1934, the provision most often used to attack insider trading in the United States. Unlike American courts, however, Japanese courts have been unwilling to broadly apply and enforce the terms of this provision. Japan's Ministry of Finance has only applied Article 58 to one case. Additionally, although Article 197 of the SEL stipulates that violations of Article 58 are punishable with as much as a three year prison term as well as a civil fine, no one in Japan has received a prison sentence for insider trading.

In addition to Article 58, SEL Article 50 regulates the management and employees of 'securities corporations' (brokers, dealers, and underwriters) and gives the Minister of Finance the authority to prohibit activities which prejudice the protection of investors, are detrimen-

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matter or which omits to state any material fact necessary to make connection with the purchase or sale of, or any other transaction with respect to, any security, or trading in securities index futures and similar tradings, trading in securities options and similar tradings, or trading in foreign market securities futures and similar tradings; or (3) make use of a false market quotation for the purpose of inducing the purchase or sale of, or any other transaction with respect to, any security, or trading in securities index futures and similar tradings, trading in securities options and similar tradings, or trading in foreign market securities futures and similar tradings.

SEL, supra note 7, art. 58.

12 The text of that law is as follows:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person in connection with the purchase or sale of any security.


14 The case of Nasu Io Kogyo is the only case to which Article 58 of the SEL has been applied. That case is significant to insider trading only in that it defined the meaning of "fraudulent device" in Article 58. The court held that term to mean "an act of deceit, that is, an act serving the defendant or another's interest, by intentionally inducing the plaintiff's justifiable reliance on his misrepresentation." Note, supra note 3, at 1298 n.14.


17 SEL, supra note 7, art. 50.
tal to the fairness of transactions, or undermine the credibility of the securities industry.\textsuperscript{18} Despite their availability, sanctions for violations of this provision also have never been invoked.\textsuperscript{19}

Finally, Article 189 of the SEL, like its United States counterpart, Section 16(b),\textsuperscript{20} prohibits "short-swing" trading by officers and directors or principal shareholders (those owning ten percent or more of a corporation's outstanding stock) and requires disgorgement of any profits should such a trade be made.\textsuperscript{21} In addition, Article 189, like section 16(b), provides for a derivative action should the corporation fail to make a demand for recovery after a specified period of time.\textsuperscript{22} However, Article 189 varies from section 16(b) in that the former has been largely ineffective at deterring short-swing insider trades, which resulted from the repeal of Article 188 in 1953.\textsuperscript{23} Article 188, an analogue of section 16(a),\textsuperscript{24} required officers and principal shareholders to report their stock holdings as well as any changes in such holdings to the Ministry of Finance. Absent this provision there was no way to effectively monitor the trading activities of such corporate insiders. That only two cases were ever brought under Article 189, as opposed to the multitude of 16(b) cases brought in the United States, demonstrates the inadequacy of the Japanese monitoring legislation.\textsuperscript{25}

In addition to the above described SEL articles, the Ministry of

\textsuperscript{18} Banoff, supra note 10, at 165.
\textsuperscript{19} See Note, supra note 3, at 1299.
\textsuperscript{21} Article 189 provides in relevant part:

(1) For the purpose of preventing an officer or a Principal Stockholder of a company from making unfair use of confidential information obtained by reason of his or its office or position in the company, if such person has realized any profits from any purchase and sale, or any sale and purchase, of his or its own account, of any Share Certificates or Similar Instruments of such company listed on a securities exchange within any period of not more than six months, such company shall have the right to demand the recovery of such profits.

SEL, supra note 7, art. 189 para. 1.
\textsuperscript{22} SEL, supra note 7, art. 189 para. 2.
\textsuperscript{23} See Note, supra note 3, at 1300. The reason cited for Article 188's repeal was its inefficiency.

The inefficiency was obviously caused by the fact that, unlike in the United States, (i) since the Japanese corporate law does not require the beneficial owner of the share to register in his own name, he could easily get away from the reporting requirement; and (ii) since article 188 did not provide for the public disclosure of the report, other shareholders could not obtain the information that could be a basis for a shareholders' derivative action.

Id. at 1300 n.26.
\textsuperscript{25} See Note, supra note 3, at 1300.
Finance employed informal administrative warnings and guidance to brokerage firms and listed companies to further stem insider trading. These informal procedures failed to achieve their stated purpose.

3. Reasons for the Failure of the Pre-1988 Law

The provisions discussed above have survived the 1988 amendments and remain largely intact. The current Japanese Diet has retained these provisions because they do not deem the provisions' failure to curtail insider trading to be attributable to an inadequacy in the language of these laws. This assessment is bolstered by the effectiveness of nearly identical laws currently in place in the United States. Perhaps these nations' varying abilities to curb insider trading can only be understood in the context of Japan's unique business and political environment and the ways in which the laws evolved in Japan.

The historical impetus for enacting these laws in Japan was entirely different than in the United States. The United States statutes were enacted as a part of a reform movement following the stock market crash of 1929. Conversely there was no internal pressure for such legislation in Japan. Instead, the Japanese laws arose as a result of the Allied Occupation. Thus, there was no real public support behind enforcing the stricter securities laws.

The Japanese business environment has differed greatly from that of the United States. The substantial volume of acquisition and takeover activity in the United States has provided an incentive to make high stakes insider trades as a way of personally maximizing the profitability of such a transaction. Public resentment against these high-rolling insider traders, such as Ivan Boesky, has led to a movement for the enforcement of insider trading laws in the United States. However, in Japan, there have been only a handful of corporate acquisitions involving unrelated parties. Thus "the impetus for stronger enforcement of insider trading laws, which largely arose in the United States as a

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26 See Zoglin, supra note 8, at 420; see also Note, supra note 3, at 1301 (for a more detailed discussion of the types of procedures used by the Ministry of Finance).
27 The Diet is Japan's parliamentary body.
28 See Zoglin, supra note 8, at 421.
29 Id.
30 Id.
31 The hostile takeovers that have dominated Wall Street are virtually nonexistent in Japan because in Japan individuals view their shareholding rights as less important than the rights of a company's workers. Because of this view, many of the shares on the Tokyo Stock Exchange are never traded. Indeed selling stock is deemed by some to be a betrayal. Given this stable shareholding system, hostile takeovers are effectively barred. See Chira, supra note 2, at D1, col. 1.
result of dramatic market movements preceding public announcement of such activity," simply has been absent in Japan.  

Japan also has different stock market related problems than the United States. Japan's Ministry of Finance has traditionally been consumed with the more prevalent problem of the manipulation of stock prices. This uniquely Japanese problem is caused by the Tokyo stock market's very thin float, which results from the stable shareholding practice among various corporate and financial institutions in Japan:

Because these institutions tend to hold each other's shares on a long term basis to promote business relationships, an estimated sixty to seventy percent of the outstanding shares on the Tokyo Stock Exchange are removed from active trading. In such a thin market, powerful investors and major brokerage firms can exert a disproportionate influence on the price of a company's shares by controlling a significant percentage of the limited floating shares.

Given the magnitude of this problem, the Ministry of Finance's decision not to enforce Japan's insider trading laws may have been the best allocation of limited resources. As Larry Zoglin has observed in his paper, Insider Trading in Japan: A Challenge to the Integration of the Japanese Equity Market Into the Global Securities Market, the much greater emphasis on insider trading in the United States may simply reflect the concerns of a market at a more mature stage of development.

In Japan there are also political obstacles to the increased enforcement of insider trading laws. It has long been alleged that Japanese politicians reap personal financial benefit by using insider information provided by those seeking political favor. The most recent example of such activity is the Recruit Scandal, which implicated many high ranking officials within the Japanese government, including associates of Prime Minister Noburu Takeshita and Finance Minister Kiichi Miyazawa. At the heart of this scandal was Hiromasa Ezoe, founder and former chairman of Recruit Co. In order to gain admission to Japan's tightknit business community, Ezoe offered extremely undervalued shares of his then unlisted subsidiary, Recruit-Cosmos Co., a real

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32 See Zoglin, supra note 8, at 421.
33 Id. at 422.
34 Id.
35 Id.
36 Id.
37 Id.
38 Id.
estate concern, to nearly 200 politicians and businesspersons. Once this subsidiary went public, these individuals were able to realize sizable gains from the sale of their stock. Government officials alone allegedly made profits ranging from 25 million to 100 million yen (about $188,000 to $752,000). Those inside the Japanese business community anonymously acknowledge that this practice is widespread, and that Ezoe’s only mistake was that he failed to be more subtle.

Japanese politicians have been unwilling to give up these lucrative activities. Their reasons are more complex than personal financial benefits, the insider activities have cemented strong relations between the securities companies and the current ruling Liberal Democratic Party. These relationships and the promise of continued financial gains virtually preclude alterations in Japan’s enforcement policy regarding insider trading regulations.

4. Reasons for the Enactment of the 1988 Amendments

Despite the myriad factors discouraging stricter enforcement of Japan’s insider trading laws, the Japanese Diet, in May of 1988, passed amendments which radically altered Japan’s regulation of insider trading. Observers cite two primary reasons for this change. The first of these is the increasing public resentment against insider traders in Japan, in part due to high publicity scandals that occurred within the past several years. The second reason is the external pressure foreign countries put on Japan to change its securities practices in order to provide a fairer market to the ever-increasing number of foreign investors participating on the Tokyo Stock Exchange. These two factors resulted in tremendous pressure on the Japanese Diet to reform Japan’s regulation of insider trading.

The domestic public pressure to change insider trading laws did not arise until September of 1987, the first time a major insider trading scandal was publicized. This scandal involved Tateho Chemical Company and Osaka-based Hanshin Sogo Bank. One month after Hanchin Sogo Bank helped rescue Tateho Chemical from financial dis-
In August of 1987, Hanshin sold off 337,000 of its Tateho shares shortly before the public announcement of Tateho's huge losses in bond futures trading. Although this transaction was investigated and securities regulators determined that Tateho had notified the bank about its corporate loss prior to its public announcement, neither party was charged with a violation. Despite public outcry and news-media criticism, Japanese authorities determined that the action did not violate existing securities regulations.

In the United States, this transaction would clearly have violated Rule 10b-5. Although SEL Article 58 contains almost identical language, Japanese securities officials were unwilling to interpret the statute as prohibiting this activity. The failure of Japanese officials to interpret the statute in such a manner gave rise to Japan's first significant public outcry over the government's inability to regulate the problem of insider trading.

This concern was further substantiated by two additional major scandals: the Sankyo Seiki/Nippon Steel scandal that occurred later in 1988 and the Recruit-Cosmos scandal mentioned above. In the first case, the share price of Sankyo Seiki Manufacturing, a music box maker, rose by ten percent a few days prior to the public announcement of the acquisition of eighteen percent of that company's shares by Nippon Steel Company, the world's largest steelmaker. An investigation by the Tokyo Stock Exchange and the Ministry of Finance revealed that as many as one hundred employees of both firms had personally profitted by trading on knowledge of the acquisition as much as a week prior to its public announcement. Again, however, no charges were brought against any of these individuals.

Finally, in the same year, the Recruit-Cosmos scandal began to unfold. Not only was the scandal newsworthy in Japan, it also received worldwide media coverage. Stories about corruption in the Japanese markets appeared nearly daily in major newspapers and television broadcasts. This coverage made the Recruit-Cosmos the most damaging

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45 See Note, supra note 3, at 1302.
46 See Jimbo, supra note 37, at 12.
47 Id.
48 See, e.g., In re Cady, Roberts & Co., 40 S.E.C. 907 (1961). This case recognized the inherent unfairness that arises when an individual uses information obtained through his special relationship with a corporation for personal gain, while he knows that the information is not available to the public. That case mandates that an individual in possession of material, non-public information must either disclose the information, or abstain from trading on it.
49 See Jimbo, supra note 37, at 12.
50 Sanger, supra note 16, at D1, col. 2. See also Jimbo, supra note 37, at 12.
51 Id.
Moreover, the Recruit situation was even more scandalous in that it implicated high level bureaucrats and government officials as well as businesspeople.

These three scandals quickly eroded Japanese public confidence in governmental ability to regulate insider trading. However, public concern within Japan over the adequacy of insider trading laws was not the only impetus behind the passage of the 1988 SEL amendments. The increasing globalization of the securities markets and the corresponding pressure it created to improve the fairness of individual marketplaces also propelled the revisions.

The enormous size and power of the Japanese stock market magnifies the impact of Japan's insider trading practices. The Tokyo Stock Exchange is currently the largest securities market in the world, having surpassed the New York Stock Exchange in volume and in market capitalization several years ago. Foreign activity in that market now comprises a significant level of all trades done, and is estimated to constitute at least seven percent of Tokyo's daily volume. Nearly every major United States securities firm now has offices in Tokyo as well as a membership with the Tokyo Stock Exchange. This indicates that "[l]ocalized capital markets are increasingly becoming internationally integrated."

As foreign participation within Japanese equity markets continued to grow, the disparity between Japanese and foreign enforcement of insider trading became a greater source of concern. Many foreign investors felt shut out of the insider-run world often referred to as "Japan Inc." To many, the market was unashamedly elitist in its approach both to Japanese and non-nationals alike who were outside the magic circle of well-connected Japanese businesspersons.

The treatment of insider trading on the Tokyo Stock Exchange was especially frustrating to American investors. Given the Securities and Exchange Commission's worldwide ban on insider trading, American traders felt handcuffed; they could not make insider trades as

52 An editorial that occurred during that time period in the respected Asahi Evening News provides evidence of this public dissent. The broadcast stressed the "need to speedily erase the impression that the Japanese stock market is an unclear market in which insider trading is rampant." Shapiro, supra note 42, at F1, col. 1.

53 Sanger, Big Board Chief Sees Shift in Tokyo, N.Y. Times, Aug. 24, 1988, at D4, col. 1. See also Chira, supra note 2, at D1, col. 1, D6, col. 2.


55 Chira, supra note 2, at D1, col. 1.

56 Note, supra note 4, at 83.

57 See Williams, supra note 38, Part V, at 2, col. 1.

58 Id.

the Japanese did, and the Japanese were unwilling to trade any other way.

Japan’s permissive attitude towards insider trading hampered all foreign investors’ abilities to fairly and accurately analyze a stock’s fundamental values and market potentials. Given that foreign investment on the Tokyo Stock Exchange benefited the Japanese economy, it was necessary at a minimum for the Japanese Diet to create the appearance of a change in policy towards insider trading so as not to discourage or diminish further foreign trades in their market.

The first political response to these pressures came in October of 1987 with the creation of a subcommittee within the Securities and Exchange Council. The subcommittee served as an advisory body to the Ministry of Finance to analyze and propose amendments to current insider trading laws. In February of 1988, this subcommittee, following intense debates, presented its report to the Minister of Finance, and within a month the report’s recommendations were incorporated into the first draft of the SEL amendments presented to the Japanese Diet. The Diet quickly passed these proposals in May of 1988. By February of 1989 the Diet had also promulgated all of the related cabinet orders and ministerial ordinances that accompanied the new laws. All of these Japanese regulations became effective on April 1, 1989.

5. THE 1988 SEL AMENDMENTS

The amendments focus on three areas. First, the new laws expand the authority of the Minister of Finance to order a company “which issues securities listed on a Japanese securities exchange to submit reports and data” to her upon request. Second, the laws impose report-
ing obligations on officers and certain stockholders of listed companies to report changes in their stock holdings. Finally, the new amendments specifically prohibit insider trading and prescribe criminal sanctions for violators.

6. EXPANSION OF THE MINISTRY'S AUTHORITY TO OBTAIN INFORMATION FROM LISTED ISSUERS

SEL Article 154 was among the original laws enacted to regulate insider trading during the Allied Occupation. This provision enabled the Minister of Finance to order a stock exchange to submit reports, “or to inspect the operations and financial position of the stock exchange for the protection of investors when he [sic] deemed it necessary.” Although this provision extended some authority to the Ministry to obtain information regarding activities on the stock exchange, the Ministry had no ability to directly investigate the issuers of stock involved in suspicious stock transactions. In reaction to this problem, the Diet amended Article 154 in 1988 to allow the Minister of Finance to directly request information from listed issuers and the stock exchange when investigating suspicious stock deals. This marked the first time the Ministry of Finance would be able to conduct direct investigations of companies involved in suspected insider stock trades. Unfortunately, this power is limited in that under the new Article 154, the Ministry itself cannot inspect an issuer’s accounting books or other documents. Instead, it can only order a company to supply data from these documents to the Ministry. In this respect, Article 154 falls short of giving the Ministry of Finance complete investigatory power, but still represents an important first step in broadening the Ministry’s investigatory power.

66 Id.
67 Id. at 83-84.
68 SEL, supra note 7, art. 154.
69 See Note, supra note 3, at 1304.
70 The amended language of Article 154 is as follows:

The Minister of Finance shall have the authority, when and if he deems it necessary and appropriate in the public interest or for the protection of investors, to order a securities exchange or an issuer whose securities are listed on such securities exchange to submit reports or data that may serve as reference material with respect to the business operations or financial condition of such securities exchange, and the authority to cause the appropriate officials of the Ministry of Finance to inspect the business operations or financial condition of, or accounting documents or other items belonging to, such securities exchange.

SEL, supra note 71, art. 154.
71 Failure to comply with a request by the Ministry to submit information can result in a fine of not more than 300,000 yen. See SEL, supra note 7, art. 206.
gatory authority.\textsuperscript{72}

7. **Reporting Requirement for Officers and Financial Shareholders**

In addition to expanding the Ministry of Finance's investigatory ability, the new amendments also require officers and principal shareholders of issuers to submit regular reports, even absent any specific Ministerial request, regarding any changes to their stock holdings.\textsuperscript{73} The new amendments essentially reinstate former Article 188, repealed in 1953, thereby empowering the Ministry to police short-swing trading by insiders more effectively.

Newly enacted Article 188\textsuperscript{74} requires officers and principal shareholders (stockholders who are beneficial owners in their own or another person's name, of at least ten percent of an issuer's total stock) to file a report with the Minister of Finance with respect to any sale or purchase of that issuer's stock made by them.\textsuperscript{75} If such purchase or sale is made through a securities company acting as a broker, the report must be filed by the securities company responsible for the transaction.\textsuperscript{76} If followed, Article 188 should provide some means of alerting the Ministry to short-swing insider trades prohibited under already existing, but previously ineffectual, Article 189.\textsuperscript{77}

Although this reporting provision represents a dramatic improvement in the monitoring of short-swing trading, it is weaker than its corresponding American Securities Exchange Act counterpart, Section

\textsuperscript{72} See Note, supra note 3, at 1310-11.

\textsuperscript{73} See SEL, supra note 7, art. 188.

\textsuperscript{74} The provision provides in relevant part:

If an officer or a Principal Stockholder (which shall mean, hereinafter through Article 190-2, a stockholder who is the beneficial owner, under his or its own name or under another person's name (including a fictitious name), of not less than 10% of the total number of issued shares of stock. . .) of a company purchases or sells. . .any share certificate, convertible bond certificate, bond certificate with warrants to subscribe for new shares or certificate representing the right to subscribe for new shares of such company listed on a securities exchange, or any option with respect to the purchase or sale transaction of any of such security. . .for his or its own account. . ., such officer or Principal Stockholder shall file, by the fifteenth (15th) day of the month following the month when such purchase and/or sale. . .occurred, a report with respect to such purchase and/or sale with the Minister of Finance. . .

SEL, supra note 7, art. 188(1).

\textsuperscript{75} SEL, supra note 7, art. 188.

\textsuperscript{76} SEL, supra note 7, art. 188(2).

\textsuperscript{77} For a discussion of Article 189, as well as a translation of its language, see supra notes 19-24 and accompanying text.
16(a),\textsuperscript{78} in two important respects. First, amended Article 188 is weaker than the original provision which was repealed in 1953. Formerly, Article 188 required directors and principal shareholders to report their securities holdings upon becoming either an officer or principal shareholder, and whenever there were changes in their holdings.\textsuperscript{79} The current version only requires filing when they sell or purchase securities.\textsuperscript{80} This weakened requirement may allow for more slippage in the amount of compliance actually achieved by Article 188. Additionally, new Article 188 (along with its corresponding provision, Article 189\textsuperscript{81}) does not provide for automatic public disclosure of all suspected short-swing trading violations. Instead, disclosure to the public only occurs after the violation is confirmed with the accused person and disclosed to the corporation.\textsuperscript{82} Public disclosure is made only if both the individual charged and the corporation fail to take action.\textsuperscript{83} The rationale for this approach was that automatic public disclosure was thought to be too stigmatizing to the alleged violator.\textsuperscript{84} The threat of such stigmatization, however, is much of what deters short-swing trades. Absent the threat of public stigma, there is no real deterrent to short-swing trading violations, since disgorgement of profits\textsuperscript{85} merely leaves the violator in the same position that person would have been in without having engaged in the transaction.\textsuperscript{86}

\textsuperscript{79} See Note, supra note 3, at 1311.
\textsuperscript{80} See SEL, supra note 7, art. 188. See also Note, supra note 3, at 1311.
\textsuperscript{81} See SEL, supra note 7, art. 189, paras. 4-9.
\textsuperscript{82} Id.
\textsuperscript{83} Id.
\textsuperscript{84} See id.
\textsuperscript{85} See Note, supra note 3, at 1311-12.
\textsuperscript{86} The method of calculating profits to be disgorged is described in Ministry of Finance Ordinance No. 40 of 1988, art. 6, translated in K. Okamura & C. Takeshita, supra note 60. Note that when multiple trades have occurred within six months, Japan does not use the lowest purchase, highest sale method of calculating profits used in the United States. Rather, they simply match the earliest purchase with the earliest sale, and so on, until purchases and sales can no longer be matched. See id. at 66-67.
\textsuperscript{88} An additional criticism was made by Tomoko Akashi in his article, The Regulation of Insider Trading in Japan. See Note, supra note 3, at 1311. Mr. Akashi noted that:

Although a director or principal shareholder must file a report through as securities company if the transaction is handled by that securities company, the principal obligation to report falls on the insider, not on the securities company. Accordingly, . . . [the SEL] does not directly impose a penalty upon a securities company for failing to report or for filing a false report.

\textit{Id.} However, this author also acknowledged that if "a securities company aids a violation by a person who has a duty to report, it can be punished as an accomplice or solicitor for violating the same provision." \textit{Id.}
The above problems associated with Article 188 will prevent it from achieving the same success section 16(a) has achieved in the United States. However, it does represent a significant improvement over prior Japanese law, which had no filing requirement for officers and principal shareholders.

8. **DIRECT PROHIBITIONS AGAINST INSIDER TRADING**

Finally, the Japanese Diet included among the new amendments two provisions which specifically prohibit insider trading — Articles 190-2 and 190-3. Corresponding penalty provisions were also drafted for a violation of either of these articles. Newly enacted Articles 190-2 and 190-3 represent Japan's first major departure from United States securities law. Unlike the broad American provisions governing insider trading, such as section 10(b) and Rule 10b-5, these new Japanese provisions specifically delineate what constitutes an insider trading offense. Article 58, unlike its United States counterpart, Rule 10b-5, was a failure in Japan. Owing in part to its vagueness, it had not been invoked to curb insider trading. With this unfortunate history, the Japanese Diet decided instead to create clear and specific prohibitions against insider trading.

Unlike Article 58 or its United States counterpart Rule 10b-5, the provisions do not require proof of scienter, and are thus easier to enforce. Proving a violation of either Article 190-2 or 190-3, requires a showing that the individual knew she was in possession of material non-public information at the time of the transaction.

These provisions, although they appear quite similar, are directed at different persons as well as different information. "Article 190-2 deals with parties related to the issuer and information generated by the issuer itself. Article 190-3 deals with parties related to the acquiring company in a tender offer and information generated outside of the

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87 See SEL, supra note 7, art. 190-2 and SEL, supra note 7, art. 190-3.
88 See SEL, supra note 7, art. 200.
89 SEL, supra note 7, art. 190-2 and SEL, supra note 7, art. 190-3.
92 See Note, supra note 3, at 1313.
93 Because of the lighter scienter requirements in Articles 190-2 and 190-3 as compared to Article 58, it would be possible in theory to violate both provisions. Should a violation of one of the specific provisions of Articles 190-2 and 190-3 be accompanied by fraudulent intent, it would be possible to violate Article 58 as well, and thus be subject to penalties under both provisions. See id.
94 See SEL, supra note 7, art. 190-2 and SEL, supra note 7, art. 190-3. See also Note, supra note 3, at 1313.
95 See Note, supra note 3, at 1306.

https://scholarship.law.upenn.edu/jil/vol12/iss2/4
target company.\textsuperscript{96}

9. \textbf{Article 190-2}

Under SEL Article 190-2, corporate insiders may not trade in the securities (including options) of the listed companies in which they are insiders if they are trading on the basis of material non-public information\textsuperscript{97} relating to that company.\textsuperscript{98} Based on this general rule, Article 190-2 looks very similar to Rule 10b-5. What makes the provision unique is the detail with which it describes its terms.

10. \textbf{Individuals Falling Within the Scope of Article 190-2}

This prohibition against insider trading extends not only to "corporate insiders" as defined by the article below, but also former corporate insiders\textsuperscript{99} who have ceased to be corporate insiders within the past year, and "tippees" (those who are "tipped" inside information).\textsuperscript{100} The Article specifically defines each of these terms. For example, "corporate insiders" are defined as follows:

(1) any officer, agent, employee or other personnel of such company. . . when he has obtained the knowledge in connection with his office;\textsuperscript{101}
(2) any principal shareholder if he has obtained material facts in connection with exercising his right to inspect the books of the corporation;\textsuperscript{102}
(3) any person who possesses statutory authority over the

\textsuperscript{96} \textit{Id.}
\textsuperscript{97} Certain stock transactions are exempt from Article 190-2's prohibition. These transactions are:
(1) the exercise of warrants;
(2) the exercise of conversation rights;
(3) purchases or sales used for defensive reasons at the order of the company's board of directors in order to fend off a tender offer or similar corporate action;
(4) purchase or sales ordered by the Ministry of Finance in order to stabilize share prices;
(5) transactions that take place outside securities markets between corporate related parties or former corporate related parties or tippees;
(6) transactions in stock that are pursuant to contracts or agreements entered into prior to when the "material facts" were obtained.

\textit{See} SEL, \textit{supra} note 7, art. 190-2, para. 5.
\textsuperscript{98} SEL, \textit{supra} note 7, art. 190-2.
\textsuperscript{99} \textit{Id.} at art. 190-2, para. 1.
\textsuperscript{100} See \textit{id.} at art. 190-2, para. 3.
\textsuperscript{101} Id. at art. 190-2, para. 1, item (1).
\textsuperscript{102} Id. at art. 190-2, para. 1, item (2).
company, when he has obtained the material knowledge in connection with the exercise of such authority. (For example, regulatory authorities given the right to inspect issuers books); 3

(4) any person, other than an Officer of the company, who has obtained material information in connection with the execution or the performance of such contract (e.g. lawyers, accountants); 4

(5) directors or others of a legal entity falling within (2) or (4) if they have obtained material facts in connection with their duties. 5

Individuals who no longer fall within any of the above five categories, but have within the past year, are classified as "former corporate insiders" under the Article and are subject to its prohibition against insider trading. 6

These five specific categories have the benefit of clearly establishing which individuals may not trade on inside information. Correspondingly, this may better deter insider trading activity. However, the law may be too limited in its scope. For example, in each of the five categories, the statute requires that the individual obtain the information "in connection with" her role as a "corporate insider." 7 By implication, the statute then appears to allow trades when the "corporate insider," as defined by the Article, obtains information outside her role with the corporation. For example, if an employee while not at work, simply overhears a conversation containing material non-public information about her company, it would appear that she could trade on this information, even with the knowledge that it was material non-public information. As the new amendments are purportedly based on general notions of "fairness," 8 it seems contradictory to allow such a transaction. If someone with an insider relationship to a corporation has information, regardless of how that information was obtained, it would seem patently unfair to allow her to trade on it if she knows it is material

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103 Id. at art. 190-2, para. 1, item (3).
104 Id. at art. 190-2, para. 1, item (4).
105 Id. at art. 190-2, para. 1, item (5).
106 Id. at art. 190-2, para. 1.
107 Id. at art. 190-2, para. 1, items (1)-(5).
108 The Diet premised their 1988 amendments to the SEL on traditional notions of "fairness," in that it is considered unfair for individuals, with special relationships to issuing companies, to trade on information to which they have special access, but which is unavailable to the public. The Diet believed that if this privileged trading was left unregulated, it would undermine the perceived fairness of the securities markets, thus destroying the trust of investors and their willingness to participate in the market. See Note, supra note 3, at 1312.
information unavailable to the rest of the investing public.

Similar limitations apply to the Article’s definition of “tippees.” To be punished as a “tippee” under Article 190-2, a tippee “must know that the tipper is a corporate-related person who has obtained the information through employment or status, that the information is of the type listed under Article 190-2... and that the information has not been disclosed to the public.” This provision forbids tippees from trading until the information is made public.

This provision, however, is hampered by several limitations. First, if neither the tipper nor the tippee trades, the provision is not violated. This situation does not exist in the United States because tippers may be liable under Rule 10b-5 for the mere act of tipping. As Japan did not implement a similarly strict law against this act, potential tipplers will remain undeterred. Moreover, under this Article, only the first tippee is subject to insider trading liability. Subsequent tippees will not be punished, unless the first tippee acts solely as a conduit. Clearly, many insider trades which most persons would view as wrong would not violate Article 190-2.

11. Definition of Material Facts

The Japanese Diet, motivated by a desire to avoid the vagueness problems associated with Article 58, drafted very specific provisions regarding the type of information deemed an Article 190-2 “material fact.” To be material, information must fall within one of the following specific provisions:

(1) a decision by the management of the company to implement any of the following or a decision by the management of said company to reverse such a decision (which has been made public):

(a) issuance of shares of stock, convertible bonds and bonds with warrants to subscribe for new shares;
(b) reduction of stated capital;
(c) stock split;

\[\text{106} \text{ See id. at 1314.}\]
\[\text{110} \text{See SEL, supra note 7, art. 190-2, paras. 3-4.}\]
\[\text{111} \text{17 C.F.R. § 240.10b-5 (1988).}\]
\[\text{113} \text{See Note, supra note 3, at 1314.}\]
\[\text{117} \text{The rationale behind this rule was that the Japanese Diet wanted to establish a bright line rule of liability that would be easy for all to follow. See id. (citing statement by Mr. Fujita, the Director of the Securities Bureau of the Ministry of Finance, House of Counselors Committee of Finance Report (15), 19-20 (May 19, 1988)).}\]
\[\text{114} \text{See id.}\]
(d) declaration of a dividend or an interim cash distribution during the fiscal year. . . provided that such dividend or cash distribution differs in terms of amount per share or method of distribution from the most recent dividend or cash distribution, as the case may be;
(e) merger;
(f) transfer to, or acquisition from, a third party, of the company’s business in its entirety or in part;
(g) dissolution (other than dissolution as a result of a merger);
(h) commercialization of a new product or new technology. . . 115

(2) the occurrence of any of the following events:

(a) damage arising out of natural disaster or business operations;
(b) change in the composition of those who constitute Principal Stockholders;
(c) event which might cause a delisting of Listed Share Certificates or Similar Instruments; . .

(3) material change in sales, operating profit or new income of said company. . . due to newly calculated projections for the company or the results of the current fiscal year as compared with the most recent projection that was previously made public (or, in the case where there is no such projection, the results of the previous fiscal year that were made public); . . . or

(4) material facts, other than facts referred to in the three preceding Items, relating to the management, business, or property of the company, which may have significant influence on the investment decisions of investors. 116

To provide even greater specificity to the law, the Ministry of Finance later passed Ministerial Ordinance No. 10 of 1989, which further delineated what constitutes a material fact under this statute. 117 The approach the Ministry adopted in this ordinance was not to define materiality, but instead to define what was not material under this law.

115 See SEL, supra note 7, art. 190-2, para. 2, item 1.
116 See SEL, supra note 7, art. 190-2, para. 2, items 2-4.
117 See Ministry of Finance Ordinance No. 10 of 1989, art. 1 and 2, translated in K. Okamura & C. Takeshita, supra note 60. This ordinance, passed on February 3, 1989, also applies to the definition of material facts provided in SEL art. 190-3.
Generally, this ordinance labels an event or corporate decision immaterial if it affects less than ten percent of the company's book value of their total assets, as of the last day in the most recent fiscal year, or ten percent of the company's sales in the most recent fiscal year. This materiality test applies to natural disasters, mergers, acquisitions, asset sales, transfers of part of the business, termination or establishment of a business affiliation, as well as other events affecting the corporation. A slightly different standard is applied to the creation of a new business or product. In these circumstances, the applicable test is whether the new business or product:

in each fiscal year which commences within three years from the beginning of the fiscal year during which the new business [or product] is scheduled to be initiated, is expected to be less than 10% of sales in the most recent fiscal year, provided that the total amount of costs specifically related to the starting-up of such new business [or product] is expected to be less than 10% of the book value of the fixed assets as of the last day in the most recent fiscal year.

(first emphasis added).

As shown above, both the Ordinance and the law itself specifically set forth what constitutes a material fact. This has the positive effect of alerting all traders as to what constitutes an offense under the new laws and allows them to alter their behavior accordingly. Alternatively, it has the problem of leaving out some situations which most would consider to be material, though not falling within the specific provisions of the law.

One major problem associated with the new definition of materiality is the Ministry of Finance's "ten percent threshold test." Many companies within Japan are simply so diverse that a rule requiring them to disclose facts affecting sales or corporate assets by ten percent or more would be inapplicable. For example, Hitachi published their

118 See id.
119 See id.
120 Id. at art. 1, item 10. This item covers the creation of new businesses. For the item which covers the starting-up of a new product, see id. at art. 1, item 6.
121 Although item 4 of paragraph 2 in Article 190-2, supra, note 116, is a catch-all provision, and thus could encompass violations that do not fit within the limits of the other specific provisions, it seems unlikely that it will be used in this manner. The Diet, in drafting such a specific law, clearly renounced the broad and vague language that led to Article 58's lack of enforcement. The preceding three items in that paragraph appear to overshadow this last provision. Although the language exists, should someone try to use it, it seems any attempted application of item 4 would yield the same poor results that Article 58 did.
sales estimates for the year ending March 2, 1990 at 3.2 trillion yen. A Hitachi official said, "I can't think of any new product that will boost our sales by more than 320 billion yen (ten percent)." 122 Certainly the development of a product, speculated to generate 319 billion yen in sales, would be considered to be a material fact by most of the investing public. Nevertheless, the current statute would classify such a development as immaterial.

An additional flaw of the present definition of materiality is that it only includes firm "corporation decisions." Thus, if an officer knows that the corporation will pass a proposal to increase capital on the following day, that person may purchase shares of the corporation's stock without being liable under the new laws for insider trading, since there has not yet been a "decision" on that matter. 123 Clearly, the investing public could regard this knowledge to be a material fact in their decision to purchase or sell stock; nevertheless, Japanese law does not treat it accordingly.

On balance, it is difficult to tell which approach yields the best results. Greater specificity certainly makes violations easier to detect. However, it problematically excludes many situations which, though not within the act's language, may nevertheless be material in the eyes of the investing public.

12. ARTICLE 190-3

Article 190-3, the counterpart to Article 190-2, regulates insider trades on information regarding tender offers. 124 This provision forbids "tender offeror insiders" of acquiring corporations from trading on information, concerning either the termination or execution of a tender offer, which they obtained through their relationship with the acquiring company, until that information is disclosed to the public. 125 As with

123 See Note, supra note 3, at 1316.
124 See SEL, supra note 7, art. 190-3.
125 Information is said to be made public when a chief executive officer or an agent authorized for that purpose discloses that information to two "news media" companies followed by a lapse of twelve hours. Under the statute, "news media" includes (a) domestic newspaper publishing companies reporting current affairs, or news agencies communicating current affairs to those publishing companies; (b) daily domestic newspaper publishing companies reporting business or economic events; or (c) the Japan Broadcasting Corporation, or other broadcasting stations. See Cabinet Order No. 23 of 1989, art. 30, translated in K. Okamura & C. Takeshita, supra note 60. Note, disclosure requirements are said to be satisfied if the information is reported to two media sources and twelve hours have elapsed, even if the information has not yet been provided to the public. Moreover, even if the information has been actually reported to
Article 190-2, individuals clause as "tender offeror insiders" are specifically defined in Article 190-3. They include:

1. any officer, agent or employee of a tender offeror when he has obtained the knowledge in connection with his office;\footnote{Id. at art. 190-3, para. 1, item 1.}
2. any stockholder of a tender offeror when he has obtained the knowledge in connection with the exercise of his right to inspect the books of the offeror;\footnote{Id. at art. 190-3, para. 1, item 2.}
3. any person who possesses statutory authority over a tender offeror, when he has obtained the knowledge in connection with the exercise of such authority;\footnote{Id. at art. 190-3, para. 1, item 3.}
4. any person, other than an officer of the tender offeror, or if the tender offeror is not a corporation, an agent or employee of the tender offeror, who has entered into a contract with the tender offeror if when he has obtained the knowledge in connection with the execution or the performance of such contract;\footnote{Id. at art. 190-3, para. 1, item 4.}
5. any officer of a corporation where such corporation is a person referred to in Item (2) or in Item (4) of Article 190-3 when he has obtained the knowledge in connection with his office.\footnote{Id. at art. 190-3, para. 1.}

Additionally, as with Article 190-2, former "tender offeror insiders" as well as "tippees"\footnote{Id. at art. 190-3, para. 4.} are subject to the same prohibitions against trading as are the above described "tender offeror insiders".\footnote{Id. at art. 190-3, para. 5.}

Unfortunately, Article 190-3 also has many of the same flaws inherent in Article 190-2. Article 190-3's definition of "tender offeror insiders" also uses the "in connection with" language which may allow the public, disclosure is not said to be satisfied if it was not based on a disclosure statement by a chief executive officer or his authorized agent. See Note, supra note 3, at 1318. Based on the above discussion, it is evident that there are serious flaws with Japanese laws regarding public disclosure under 190-2 and 190-3. Perhaps a better approach would be to eliminate the requirement that the information must be based on an official disclosure statement, and instead simply require that the information actually be reported to the public by two qualifying media. This approach would better satisfy the true spirit of the reporting requirement, i.e. to ensure that the public is basing their trades on the same information available to those inside the corporation.\footnote{In paragraph 6, Article 190-3 is also made subject to exemptions similar to those that are listed in paragraph 5 of Article 190-2. See supra note 97.}
for some transactions which appear objectionable on fairness grounds. Additionally, Article 190-3 is governed by the same Ministerial Ordinance defining immateriality as Article 190-2. Thus, if a tender offer affects less than ten percent of an acquiring company's book value of its total assets or ten percent of its sales, it is considered immaterial, and trades regarding such a tender offer would be permitted prior to any public disclosure of the deal. As previously noted, a tender offers affecting nine percent of the total sales or assets of a large and diversified corporation could be considered material to the investing public. Nevertheless, Japanese law does not require disclosure prior to trading on such information.

13. PENALTY PROVISIONS

Finally, the Japanese Diet enacted penalty provisions for failure to comply with both Articles 190-2 and 190-3. Newly drafted Article 200 stipulates that Article 190-2 or 190-3 violators can receive up to six months imprisonment with a requirement of labor, or a fine not to exceed five hundred thousand yen. Unlike Article 189, Articles 190-2 and 190-3 do not provide for civil remedies — insider traders who violate either of these provisions are not required to disgorge their profits. The justification for this is that neither of these provisions requires a showing of culpability, thus stricter penalties are unwarranted. The end result, however, is that violations of either Articles 190-2 or 190-3 are only mildly sanctioned. As insider trades can potentially reap huge profits, the five hundred thousand yen fine and six months sentence may provide little deterrence against this activity, particularly since traders are currently allowed to keep their profits.

The Japanese, however, are not unaware of the problems inherent in their penalty structure. Discussions concerning the availability of civil remedies occurred during the drafting of the new 1988 Amendments. Nevertheless, upon recommendations by the Securities Exchange Council, it was decided that this issue should be postponed pending further study. Some Japanese commentators have recommended re-

184 See supra notes 108-09 and accompanying text.
185 See Ministry of Finance Ordinance No. 10 of 1989, translated in K. Okamura & C. Takeshita, supra note 60.
186 Id.
187 SEL, supra note 7, art. 200.
188 See Note, supra note 3, at 1315 n.168, citing Securities Exchange Council Report, Naibusha torihiki no kisei no arikata ni tsuite [Ways to Regulate Insider Trading], Feb. 24, 1988, which stated that "[m]easures should be taken to ensure the effectiveness of civil damages payable to . . . [aggrieved parties]. However, with respect to the concept of damages sustained through . . . [transactions] occurring on the stock
quiring disgorgement of profits and compensation to aggrieved parties in lieu of criminal penalties for Articles 190-2 and 190-3 violations.139 The Securities Law may thus be further amended at some future point in order to provide for such remedies. Until then, unfortunately, the effectiveness of Articles 190-2 and 190-3 may be hampered by inadequate penalty provisions.

14. PROBABLE IMPACT OF THE NEW AMENDMENTS

As evidenced by the above discussion, Japan’s new SEL amendments are extensive.140 For the first time in Japanese history, the Diet has made substantial efforts to deter insider trading. Though the new articles are not problem-free, there is reason to hope for some change in Japan’s treatment of insider trades.

15. EVIDENCE THAT THE LAW MAY BE EFFECTIVE

Indeed there is evidence that those who participate in the Japanese market are beginning to take the new laws seriously. Major brokerage houses in Japan have begun to put up “Chinese Walls” to block the flow of information between their corporate finance and retail brokerage sections.141 Such devices prohibit investment bankers from discussing their business deals with traders participating on the stock exchange, and thus provides one good means to help prevent insider trading, if traders cannot get inside information, they cannot make inside trades.

United States brokerage houses have been using these “Chinese Walls” for decades to separate investment bankers and floor traders. However, until recently, “Japanese securities houses combined the function of corporate investment banker and portfolio manager in one division - sometimes even in one person.”142 This system made insider exchange, further study is required with regard to the standing of the plaintiff and procedure of the lawsuit. Thus, it is necessary to tackle the issue as a long-term task.”

139 See Note, supra note 3, at 1315.

140 On a visit to Tokyo, in 1988, David Ruder, chairman of the United States Securities and Exchange Council stated that the amended Securities and Exchange Law covered “98% of what we cover in the United States.” Jimbo, supra note 37, at 12.

141 See Jimbo, supra note 37, at 12, col. 3. Nomura Securities, Japan’s largest securities firm, created a “Chinese Wall” in August, 1988. See Sanger, supra note 16, at D1, col. 3.

142 Sanger, supra note 16, at D5, col. 2. “If one person was in charge of Hitachi, for example, he would oversee raising funds for Hitachi and also investing Hitachi’s holdings.” Id. This structure made the practice of insider trading an almost irresistible temptation.
trading virtually inevitable.

There is hope that the implementation of "Chinese Walls" will help eliminate the temptation to engage in insider trades. Indeed some speculate that "Chinese Walls" will be "shockingly effective," as in most firms, the penalty for violating a "wall" will be dismissal. As a director of Nomura Securities noted, "this is a strong penalty in a country where lifetime employment is everything and a dismissed employee stands little chance of being hired elsewhere."

In addition to the implementation of "Chinese Walls" there is other evidence that the Japanese are not taking these amendments lightly. For example, companies within Japan have become increasingly cautious about giving information to stock analysts. Although existing law requires listed companies to disclose some details of their performance to analysts, some analysts are now denied access to information which was previously willingly disclosed due to fears of violating anti-disclosure laws absent the requisite public disclosure the new statutes prescribe. Although these companies may be accused of overreacting, this at least provides optimism for those hoping that the new amendments are not disregarded like the old laws.

Finally, the Ministry of Finance has also taken affirmative steps to help ensure the new laws' enforcement. In July of 1989, the Ministry appointed a special task force within its securities bureau to tighten supervision over Japanese stock market activity, and to investigate all future allegations of insider trading. Admittedly, this will still leave the resources of Japan's supervisory teams behind those of the United States. Nevertheless, it is hoped that the appointment of this new task force will "go some way to answering criticism from the United States and Europe that its rules on stock market behavior" and the enforcement of such rules are too lax.

16. REASONS TO DOUBT THE LAWS' SUCCESS

Despite the foregoing discussion, optimism about the amendment's probable reduction of insider trading should be guarded for two rea-
sons. First, Japan is not a very litigious society, and thus may be unwilling to vigorously enforce the recent legislation. This would certainly be consistent with historical Japanese practices in this area. Secondly, and more importantly, the prevalence of insider trading in Japan reflects Japanese cultural and business norms which may be too securely institutionalized to be altered by the new laws.

While the historical failure of insider trading laws "might be attributed to the fact that most Japanese do not think there is anything wrong with insider trading," that is at best only a partial explanation. Japan's failure to enforce these laws is a manifestation of fundamental Japanese attitudes towards law and litigation. Not only have past insider trading laws been ignored, there has been "almost no public or private enforcement of any of the provisions of the securities law in Japan, whether or not they involve insider trading."

"The Japanese rarely litigate, nor do they use lawyers very often." In 1984 Japan had only 12,000 lawyers; per capita this represented only one-seventeenth of that in the United States. In 1982 alone, "the California state courts heard more than eleven times as many civil cases, on a per capita basis, than did those of Japan."

Similarly, the per capita number of civil lawsuits in the United Kingdom and West Germany, respectively, approximately ten and twelve times that of Japan in the same year. In the securities area this difference has been even more extreme. Japan has seen only one private action litigated under any of its Securities and Exchange Laws, and the Ministry has never brought an action for injunctive relief. In contrast, in the period between 1966 and 1973, there were at least 2,292 private securities actions brought in the Southern District of New York alone.

Two primary theories have been used to explain this striking lack of litigation:

One view is that the Japanese culture values harmony and conciliation; litigation is a threat to this cultural norm. A variation on the 'cultural norm' explanation attributes the
lack of civil litigation to a sharp traditional division between
the public and private spheres in Japan; private civil litiga-
tion simply is not used to enforce public goals.159

A second theory is that Japan’s institutional barriers to litigation
render it unprofitable.160 For example, in Japan, the securities laws
cannot be enforced through a class action.161 Class actions, however,
may represent the only economically feasible means to bring an insider
trading suit.162 Individual shareholders are simply not likely to be will-
ing to bear the huge costs of litigation, particularly given that they may
have little to gain through victory. Moreover, if an individual bringing
a securities suit loses, the individual would be forced to pay all the legal
costs incurred as Japan prohibits no contingent legal fees163 — thus
providing an additional deterrent to securities litigation. Potential Japa-
nese litigants also suffer from limited discovery and a shortage of both
lawyers and judges.164

A noted Japanese scholar suggested that as Japan becomes in-
creasingly urban and industrial, litigation may become more respecta-
ble and barriers to it may fade.165 Until that time, however, it seems
unlikely that the new insider trading laws will be enforced with any
more vigor than the old laws. As long as the Japanese are unwilling to
take their violators to court, little will be done to curb insider trading.

Additionally, and more importantly, there are strong cultural
norms which may hinder the laws’ ability to stop insider trading. In-
sider trading is simply not viewed as wrong by many of the participants
in Japan’s securities markets, rather it is viewed as a normal means of
conducting business. One stock analyst anonymously remarked that
“there’s a completely different attitude about information . . . [in Ja-
pan]. The idea that information should be available equally to everyone
is quite a revolutionary idea.”166

Japan is simply a different society. It has always been an insider
society where “the rights of the insider - the tight-knit village, the clan,
the alumni class - always have been paramount.”167 Confidential infor-

159 See id. at 168.
160 See id.
161 See id.
162 In the United States, class actions are by far the most common means used to
enforce securities laws violations.
163 See Banoff, supra note 10, at 168.
164 See id.
165 See id.
166 Hiatt & Shapiro, supra note 1, at A42, col. 1.
167 Id. (quoting Naohiro Amaya, a former top bureaucrat and respected Japanese
commentator).
mation is often shared among tight interlocked groups of businesspeople in order to cement their business relationships. This sharing of inside information may be a prerequisite to entering Japan's closed and elite business groups.\textsuperscript{168}

To most familiar with Japanese culture, it is unthinkable that the new laws will have much impact in deterring this prevalent and widely accepted activity. This practice of "gift giving" is simply too deeply ingrained in Japanese society.

Politicians, manufacturers, financiers, and employees all pull together for Japan's advancement. . . . They throw business to each other. . . . And they quietly look the other way when a questionable gift is given, a product's price is fixed, a stock is manipulated, or a bit of inside information is passed along.\textsuperscript{169}

Securities brokers have ascended the corporate ladder by exchanging inside information with their colleagues from the moment they graduated from college:\textsuperscript{170} "[t]he idea that they will stop swapping the information that has been the lifeblood of their work, one Japanese broker said with some understatement 'strains credulity.'"\textsuperscript{171}

17. CONCLUSION

The recent, widely publicized scandals in Japan manifest Japan's changing attitude toward insider trading.\textsuperscript{172} This change and the enactment of the 1988 SEL amendments are cause for optimism concerning the potential decline of insider activity in the Japanese markets. The law, however, is hampered by flawed language and the cultural institutionalization of insider trading as business etiquette. Traditionally, Japan has been an insider society, and consequently, insider trading is not perceived to be wrong. Rather, most view it as a necessary component to successfully conducting affairs in Japan's tightly knit business community.

Thus the new law must not only end an extremely prevalent practice in a society which rarely seeks to enforce its laws, but to be truly effective it must also change Japanese views regarding the acceptability of insider trading. This may be an insurmountable task. For a nation such as Japan, which must also overcome a history of unenforced se-

\textsuperscript{168} Id.
\textsuperscript{169} Yemma, \textit{supra} note 40, at 11.
\textsuperscript{170} See Sanger, \textit{supra} note 16, at D1, col. 3.
\textsuperscript{171} Id.
\textsuperscript{172} See \textit{supra} notes 44-52 and accompanying text.
securities laws, the total realization of these goals may be unachievable. The law may, however, help start to erode the Japanese institutionalization practice of insider trading. At a minimum the amendments represent an affirmative step towards eliminating the "insider’s heaven" that currently exists on Japanese stock exchanges.