

EFFECTIVE ENFORCEMENT FOR INVESTOR PROTECTION: INJUNCTION UNDER THE JAPANESE AND THE U.S. SECURITIES REGULATIONS

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Abstract

An injunction is a judicial procedure for investor protection where the administrative organization and the court cooperate very closely. In Japan, injunction is recently expected to be more greatly utilized. Court decisions, however, misconstrue the requirements for granting a motion of injunction and need to be corrected. Additionally, other measures supplemental to injunction are needed for investor protection to be more effective. This article offers viable answers to the said needs.

Table of Contents

- I. Introduction
- II. Injunction
 - 1. JFIEA § 192
 - 2. US Securities Act § 20 (b)
- III. First Decision to Grant an Injunction under JFIEA: *The Case of Daikyo, Inc.*
- IV. Discussion & Analysis
 - 1. Critique of Court Decisions: Requirements for Injunction
 - (1) Considered individually or comprehensively?
 - (2) A substitute to administrative relief?
 - (3) Meaning of “urgent necessity” and “necessary and appropriate for public interest and investor protection”
 - 2. Injunction against Wrongful Acts Violating JFIEA § 157
 - 3. Rescission or Change of Injunction under JFIEA § 192 (2)
 - 4. Revision of JFIEA § 187: Supplemental Measure to Injunction
 - 5. Disgorgement
- V. Concluding Caveat

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I. Introduction

Deriving from the US Securities Act of 1933 and the Securities Exchange Act of 1934, the Japanese Securities Exchange Act (“JSEA”) was enacted in 1948. JSEA was wholly reformed into the Japanese Financial Instruments and Exchange Act (“JFIEA”) on September 30th, 2007.

JFIEA § 1 stipulates “protection of investors” as one of its legislative aims.¹ Recently, JFIEA was partially revised and the Financial Alternative Dispute Resolution System (“FADRS”) was introduced into JFIEA in order to enhance protection of investors. Based on FADRS, fair institutions, approved by the Japanese Financial Services Agency (“JFSA”),² are expected to promptly propose adequate resolutions to disputes between investors and securities companies.³ However, because class action lawsuits have not yet been institutionalized in the Japanese legal system, after-the-facts lawsuits seeking compensatory damages are not regarded as sufficiently effective to realize strong investor protection. Thus, preventive measures against illegal acts are urgently needed for the protection of investors.⁴ As one of these preventive measures, practitioners have recently started paying attention to “injunction under JFIEA § 192,”⁵ especially after the Tokyo District Court granted a motion for injunction:⁶ the Japanese

¹ The Financial Instruments and Exchange Act § 1 provides as follows:

The purpose of this Act is, . . . by developing systems for disclosure of corporate affairs and other related matters, providing for necessary matters relating to persons who engage in Financial Instruments Business and securing appropriate operation of Financial Instruments Exchanges, to ensure fairness in . . . issuance of the Securities and transactions of Financial Instruments . . . and to facilitate the smooth distribution of Securities, as well as to aim at fair price formation of Financial Instruments . . . through the full utilization of functions of the capital market, thereby contributing to the sound development of the national economy and *protection of investors*.

(Emphasis added)

By Japanese Law Translation,

<http://www.japaneselawtranslation.go.jp/law/detail/?id=1911&vm=04&re=01>.

For another published English translation of JFIEA, see the following:

The purpose of this Law shall be to make issuance of securities and trades . . . of financial instruments, . . . to be carried out in fair and to ensure adequate liquidity to securities, as well as to make fair price formation . . . of financial instruments . . . through fulfillment of full functions of capital markets by developing disclosure system of corporate affairs . . . and by stipulating necessary matters for person who performs financial instruments dealing business and assuring appropriate management of financial instruments exchange with the view to contributing to the development of healthy national economy as well as *protection of investors*.

(Emphasis added)

“The Financial Instruments and Exchange Law of Japan,” EHS Law Bulletin Series vol. 6 (Eibun-Horei-Sha, Inc., 2007).

² For details about JFSA, see *infra* “II. 1 JFIEA § 192.”

³ For the author’s evaluation of this reform, see, Hiroyuki Ogawa, “The Analysis of ‘Doctrine of Manifest Disregard of the Law’ in U.S. Securities Arbitration and the Implication for the Financial Alternative Dispute Resolution in Japan,” 73 *Shoken keizai kenkyu* 121 (2011).

⁴ For the author’s opinion on institutionalizing U.S.-type securities class action lawsuits into the Japanese legal system, see, Hiroyuki Ogawa, “Reform of Securities Class Action Lawsuits in U.S. and Its Political Implication for Japan,” in *New Developments in Corporate Law and Financial Law* 15 (Chuokeizaisha, 2009).

⁵ Injunction under the Japanese Corporate Act also can and must be utilized for protecting shareholders. Hiroyuki Ogawa, “Corporate Restructuring and Protection of Minority Shareholders,” 43 *Asia University L. Rev.* 1 (2009).

⁶ For this decision, see *infra* “III. First Decision to Grant an Injunction under JFIEA: *The Case of Daikyo, Inc.*”

Securities and Exchange Surveillance Commission (“JSESC”)⁷ filed a motion for injunction based on JFIEA § 192 in 2010 for the first time since JSEA was enacted in 1948. Injunction under JFIEA § 192 is highly expected to play a critical role in ensuring market integrity and investor protection. This article analyzes and discusses the significance, issues, and proposals of injunction under JFIEA § 192.

II. Injunction

1. JFIEA § 192

Injunction under JFIEA § 192 finds its origin in the Securities Act of 1933 § 20(b).⁸ JFIEA § 192, whose title reads “Prohibition Order or Order for Suspension Issued by Court,” provides as follows:⁹

(1) When a court finds that there is an urgent necessity and that it is necessary and appropriate for the public interest and protection of investors, it may give an *order* to a person who has conducted or will conduct any act in violation of this Act or orders issued under this Act *for prohibition or suspension of such act*, subject to filing of a petition by the Prime Minister or by the Prime Minister and Minister of Finance.

(2) A court may rescind or change the order issued under the provisions of preceding paragraph.

...

(Emphasis added)

Injunction under JFIEA § 192 is effective because it can be used for preventing future illegal acts, but it has not been applied until recently.¹⁰ One of the reasons for this non-application is that it would take a lot of time for the court to grant a motion for injunction.¹¹ The legislative aim of injunction under JFIEA § 192 is to ensure protection of investors by virtue of stopping illegal and damaging acts practiced against them.¹² If the injunction order is highly reported,

⁷ For details about JSESC, see *infra* “II. 1 JFIEA § 192.”

⁸ Hideki Kanda, Nomura Securities Department of Law & Kazuo Kawamura, *Commentary on Securities Exchange Law* 1329 (Yuhikaku, 1997). For a discussion on the Securities Act of 1933 § 20(b), see *infra* “II. 2 US Securities Act § 20 (b).”

⁹ Another translation by *EHS Law Bulletin Series*, *supra* note 1, states as follows:

If a Court deems it urgently required and also necessary and appropriate in the public interest and for protection of investors, it may *order* a person who has violated or is about to violate this Law or an order based thereon *to prohibit or suspend such act* upon petition from the Prime Minister or the Prime Minister and the Minister of Finance.

2. The Court may rescind or change an order issued pursuant to the preceding paragraph.

...

(Emphasis added)

¹⁰ Etsuro Kuroshima, *Financial Instruments and Exchange Act*, 4th ed. 225-226 (Nihon Keizai Shuppansha, 2011).

¹¹ Mitsuo Kondo, Kazushi Yoshiwara & Etsuro Kuroshima, *Primer on Financial Instruments and Exchange Act* 500 (Shoji Houmu, 2009).

¹² Seiji Tanaka & Wataru Horiguchi, *Commentary on Securities Exchange Act*, revised ed. 1118-19 (Keiso Shobo,

one would expect it to function as a strong warning to the public against illegal acts.¹³

As it is difficult to prove that somebody is about to engage in an illegal act, an injunction will be issued in most cases when somebody is proven to have engaged in an illegal act or to be engaging in such act.¹⁴ One commentator argues that issuance of an injunction can be used as evidence of the existence of an illegal act in civil action for compensatory damages.¹⁵

Similar to injunction under JFIEA § 192, the Japanese Commodity Futures and Exchange Act (“JCFEA”) § 328 also provides this injunction.¹⁶ But, unlike JFIEA § 192, the proof of existence of “irrecoverably damaging circumstances” is required for granting a motion of injunction under JCFEA § 328.¹⁷

The 2008 revision of JFIEA § 194-7 (4) delegates the power to file a motion of injunction to JSEC which is expected to exercise its delegated powers effectively and promptly.¹⁸ The investigative powers under JFIEA § 187 for filing a motion of injunction is also delegated to JSEC.¹⁹

JSEC was established as an external bureau attached to the Japanese Ministry of Finance (“JMOF”) under JSEA amended in May 1992. JSEC became a part of JFSA when JFSA was

1996). A commentator attaches importance to “public interest,” which differs from the “collective interest of individual investors.” See Kanda, Nomura & Kawamura, *supra* note 8, at 1334. For a discussion and analysis of “public interest” and “investor protection,” see *infra* “IV. 1 (3) Meaning of ‘urgent necessity’ and ‘necessary and appropriate for the public interest and investor protection.’”

¹³ Katsurou Kanzaki, *Securities Exchange Act*, 2nd ed. 580 (Seirin Shoin, 1987).

¹⁴ Kouichi Miyamoto, “Inspection of Funds—Latest Trend,” 305 *Monthly Capital Market* 24, 32 (2011).

¹⁵ Sadakazu Osaki, “Utilizing Temporary Restraining Order,” *Financial Information Technology Focus* 8, 9 (November 2011).

¹⁶ JCFEA § 328, whose title is “Prohibition order by the court,” states as follows:

- (1) The court may issue an order to prohibit acts violating this Act to a person who has committed or intends to commit said acts, when there is an *urgent necessity* and the court finds it *necessary and appropriate for protecting public interest*, upon a motion of the competent minister.
 - (2) A prohibition order set forth in the preceding paragraph shall be issued only in the case where unrecoverable situations have occurred and shall be revoked immediately when the necessity has disappeared.
 - (3) The court may rescind or change an order issued pursuant to the provisions of the preceding paragraph.
 - (4) Cases prescribed in paragraph (1) and the preceding paragraph shall fall under the jurisdiction of a district court in the place where the respondent’s domicile is located.
 - (5) Judgment prescribed in paragraph (1) and paragraph (3) shall be carried out pursuant to the Non-Contentious Cases Procedure Act. . . .
- (Emphasis added)

By Japanese Law Translation,

<http://www.japaneselawtranslation.go.jp/law/detail/?id=1899&vm=04&re=01&new=1>.

¹⁷ For the detailed difference in requirements for injunction between JFIEA and JCFEA, see Hiroyuki Ogawa, “Regulation and Integrity of the Japanese Commodity Futures Market—Guidance from the U.S. and European Market Surveillance Institutions (1): the U.S. Commodity Futures Trading Commission,” <http://www.jcfia.gr.jp/study/ronbun-pdf/no16/100.pdf> at 18-19.

¹⁸ Tomonobu Yamashita & Hideki Kanda, *Outline of Financial Instruments and Exchange Act* 456 (Yuhikaku, 2010); Yuichi Ikeda, Hidenori Mitsui, Naohiro Masuda, Hideki Itou, Tatsufumi Shibata & Masahiko Saito, *Commentary on the 2008 Revision of Financial Instruments and Exchange Act*, 406-408 (Shoji Houmu, 2008). It is reported that JSEC will be more active in filing motions for injunction. *Nihon Keizai Shinbun*, February 28th, 2008, at 1.

¹⁹ For further discussion and analysis about § 187, see *infra* “IV. 4 Revision of JFIEA § 187: Supplemental measure to injunction.”

created in June 1997 in response to widespread calls for administrative reform at JMOF. JSESC is granted enforcement and audit powers to investigate conduct that is detrimental to the integrity of the market. JSESC, however, does not have prosecutorial power and must currently report offenders to the prosecutor's office. Therefore, most of JSESC's market enforcements are conducted through its inspections of securities companies. JSESC has been active in reporting offenders to the prosecutorial authorities and in issuing recommendations on administrative actions to JFSA.²⁰ For instance, administrative penalties were imposed for recommendations of administrative monetary penalty payments as a result of inspection of insider trading in fiscal 2006.²¹ The JFSA took over responsibility from JMOF for planning of the financial system in July of 2000.²²

The 2010 revision of JFIEA § 194-7 (7) makes it possible for JSESC to re-delegate to the commissioner of a finance bureau the powers to investigate and to file a motion of injunction. The district court, which grants a motion of injunction, does not have the power to enforce its decision on its own,²³ but the criminal penalty under JFIEA § 198 (viii) will be imposed by another court on the violator of the said injunction. Additionally, the 2010 revision of JFIEA § 207 (1) (iii) introduces concurrent imposition of criminal penalty on a corporation and its directors, and raises the potential criminal fine against such corporation to 300 million yen. These revisions to criminal clauses have enhanced the effect of injunction.²⁴

2. US Securities Act § 20(b)

The US Exchange Act of 1933 § 20 (b), which gives the Securities and Exchange Commission the power to bring an action for injunction and is also the model code for JFIEA § 192, provides as follows:

Whenever it shall appear to the [Securities and Exchange] Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this title, or of any rule or regulation prescribed under authority thereof, *the Commission may in its discretion, bring an action* in any district court of the United States, . . . *to enjoin such acts or practices*, and upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond.

(Emphasis added)

The US Securities and Exchange Act § 21 (d), whose title reads “Injunction Proceedings; Authority of Court to Prohibit Persons from Serving as Officers and Directors; Money Penalties in Civil Actions” and which is similar to the US Exchange Act of 1933 § 20 (b), provides as

²⁰ Christopher P. Wells, “Financial Services and Regulation,” in *Japanese Business Law* 567-568 (Gerald Paul McAlinn, ed. 2007).

For other materials explaining the role and function of JSESC, see <http://www.fsa.go.jp/sesc/english/aboutsesc/all.pdf>, <http://www.fsa.go.jp/sesc/english/reports/re2009.pdf>.

²¹ Japan Securities Research Institute, *Securities Market in Japan 2008* 335 (2008).

²² Wells, *supra* note 20, at 556.

²³ Tanaka & Horiguchi, *supra* note 12, at 1118-19.

²⁴ Hiroaki Takahashi & Masafumi Yahara, “Outline on Reform of Financial Instruments and Exchange Act,” 1900 *Shoji Houmu* 11 (2010).

follows:

(1) Whenever it shall appear to the [Securities and Exchange] Commission that any person is engaged or about to engage in any acts or practices constituting a violation of any provision of this title, the rules or regulations thereunder, . . . *it may in its discretion bring an action* in the proper district court of the United States, . . . *to enjoin such acts or practices*, and upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond.

(Emphasis added)

The test generally applied for granting an injunction is whether there exists a reasonable likelihood that the defendant will engage in wrongful acts if he or she is not thus enjoined.²⁵ In deciding whether there exists the reasonable likelihood mentioned above, the Court of Appeals for the Second Circuit regards as factors to be considered “the degree of scienter involved, the sincerity of the defendant’s assurances against future violations, the isolated or recurrent nature of the infraction, the defendant’s recognition of the wrongful nature of his conduct, and the likelihood, because of the defendant’s professional occupation, that future violations might occur.”²⁶ Other factors, such as the gravity of the offense and the adverse effect on the defendant,²⁷ are also to be considered in granting a motion of injunction. In *Aaron v. SEC*,²⁸ the US Supreme Court held that SEC is required to prove the existence of scienter in order to obtain an order of injunction based on the Securities Exchange Act § 10 (b)²⁹ and Rule 10b-5³⁰ promulgated thereunder. Chief Justice Burger noted that “[a]n injunction

²⁵ *SEC v. Advance Growth Capital Corp.*, 470 F.2d 40, 53 (7th Cir., 1972). See also Ogawa, *supra* note 17, at 13-16.

²⁶ *SEC v. Universal Major Indus. Corp.*, 546 F.2d 1044, 1048 (2d Cir., 1976).

²⁷ *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1102 (2d Cir. 1972).

²⁸ 446 U.S. 680 (1980).

²⁹ The U.S. Securities and Exchange Act § 10, under the title of “Regulation of the use of manipulative and deceptive devices,” provides 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. . . .

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as *necessary or appropriate in the public interest or for the protection of investors*.

...

(Emphasis added)

³⁰ The U.S. Securities and Exchange Act Rule 10b-5, under the title of “Employment of Manipulative and Deceptive Practices” provides 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,

(a) To employ any device, scheme, or artifice to *defraud*,

(b) 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

(c) 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.

(Emphasis added)

is a drastic remedy, . . . and should not be obtained against one acting in good faith.”³¹ Prof. Steinberg, however, argues that “the absence of scienter may not preclude the granting of such relief where the applicable statutory provision requires only negligent culpability.”³²

The court can later dissolve or modify the injunction order by weighing “the severity of the alleged danger which the injunction was designed to eliminate against the continuing necessity for the injunction and the hardship brought by its prospective application.”³³ With respect to the factors to be considered for dissolution and modification, Prof. Steinberg further proposes such factors to be “subsequent change of fact or law,” “the extent of adverse, unforeseen collateral consequences,” “whether the injunction has fulfilled its objectives,” “whether the individual deterrent effect of the injunction has ceased,” “the decree’s effect on societal deterrence,” and “the extent and nature of the public or other countervailing interest involved.”³⁴

III. *First Decision to Grant an Injunction under JFIEA:* The Case of Daikyo, Inc.

This is the first case where an injunction to suspend acts is issued under JFIEA § 192 since JSEA, former act preceding JFIEA, was enacted in 1948.³⁵ JSEC filed a motion for injunction under JFIEA § 192 against Daikyo, Inc., its representative director, and other directors (“Defendants”) at the Tokyo District Court on November 17th, 2010, alleging that the Defendants, without being registered with JFSA, were soliciting prospective investors for shares and stock options (“Stocks”) of Seibutsu-Kagaku Research, Inc.³⁶ in the course of trade and

³¹ 446 U.S. at 703.

³² Marc. I. Steinberg, *Understanding Securities Law* 418 (LexisNexis, 2007). See also *SEC v. Washington County Utility District*, 676 F.2d 218 (6th Cir., 1982); *SEC v. Murphy*, 626 F.2d 633 (9th Cir., 1980).

³³ *SEC v. Warren*, 76 F.R.D. 405, 408 (W.D. Pa. 1977), *aff’d*, 583 F.2d 115 (3d Cir., 1978).

³⁴ Steinberg, *supra* note 32, at 422-23.

³⁵ 2104 *Hanrei Jiho* 130 (2011); 1357 *Kinyu Shoji Hanrei* 28 (2011).

³⁶ Arguing that the non-registered offering of securities by Seibutsu-Kagaku Research, Inc. violated JFIEA § 4(1), JSEC additionally filed a motion for injunction at the Kofu District Court on November 26th, 2008.

JFIEA § 4 (1) provides as follows:

An offering of securities . . . or secondary distribution of securities . . . shall not be made unless *the issuer has made notification* with Prime Minister for the said offering or secondary distribution of the said securities. . . .

(Emphasis added)

The Court granted the motion on December 15th, 2010 (unpublished opinion).

http://www.fsa.go.jp/sesc/news/c_2010/2010/20101216-1.htm.

For another unpublished opinion by the Tokyo District Court on the *Case of Benefit Arrow, Inc.* on July 5th and 15th in 2011, respectively, see

http://www.fsa.go.jp/sesc/news/c_2011/2011/20110705-2.htm,

http://www.fsa.go.jp/sesc/news/c_2011/2011/20110715-3.htm.

Additionally, on December 22nd, 2011, JSEC filed a motion in the Tokyo District Court for prohibiting E-Factory and Excellent, Inc. from engaging in practices violating JFIEA § 38 (i), which provides that a financial instruments business operator, etc. or officers or employees thereof shall not conduct an act of providing a customer with false information concerning the conclusion of a contract for financial instruments transaction or solicitation thereof. The Court granted the motion on February 3rd, 2012.

http://www.fsa.go.jp/sesc/news/c_2012/2012/20120203-1.htm.

were thereby in violation of JFIEA § 29.³⁷ Finding that none of the Defendants are registered as a Financial Instruments Business Operator under JFIEA § 29, the Court granted a motion of injunction on November 26th, 2010. The Court states as follows:

Seibutsu-Kagaku Research, Inc. issued Stocks five times in total from February to June in 2010. The Defendants solicited general investors into purchasing the Stocks, which fell under the “Solicitation for Acquisition” specified in JFIEA § 2 (3) (iii). One hundred and twelve general investors paid 98.85 million yen in total for the shares and received 2,630 shares. Eighty-nine general investors acquired 1,965 stock options. The Defendants earned 32.95 million yen as handling fees.

Besides, Seibutsu-Kagaku Research, Inc. prepared for additional stock issue, setting the due date of payment as November 30th, 2010. The Defendants also solicited general investors into purchasing the said shares. Seibutsu-Kagaku Research, Inc. was ready to issue two hundred shares to the five investors who had already accepted the offering. Furthermore, the Defendants admitted that they repeatedly solicited shares of four companies other than Seibutsu-Kagaku Research, Inc.

The Kanto Regional Finance Bureau of the Ministry of Finance (“KRFB”), receiving reports from general investors, launched an investigation through a written inquiry sent to the Defendants on March 2, 2010. KRFB issued a warning to suspend their acts on March 25 as the Defendants admitted that they were performing such acts that would fall under the “Financial Instruments Business” defined in JFIEA. The Defendants did not terminate the said actions although they promised to do so by responding to the warning issued by KRFB on April 5.

The Stocks of Seibutsu-Kagaku Research, Inc. fall under “Securities” (JFIEA § § 2(1)(ix), 2(2)). The acts to solicit the Securities fall under “Dealing in Public Offering or Private Placement of Securities” (JFIEA § 2(8)(ix)), and the acts performed in the course of trade also fall under “Financial Instruments Business” (JFIEA § 28 (1) (i)) which shall be conducted only by persons registered under JFIEA § 29. The Defendants, however, were not registered and were therefore obviously in violation the said article of JFIEA.

Because administrative relief, e.g., JFIEA § § 51³⁸ and 52,³⁹ is not

³⁷ JFIEA § 29 provides as follows:

Any business of financial instruments transactions shall be performed only by *the person who obtains the registration* from the Prime Minister.

(Emphasis added)

³⁸ JFIEA § 51, under the title of “Order to improve business operation to a financial instruments business operator,” provides as follows:

When the Prime Minister finds it *necessary and appropriate for the public interest or protection of investors*, with regard to a Financial Instruments Business Operator’s business operation or the status of its property, he/she may order said Financial Instruments Business Operator to change the methods of business or take other necessary measures for improving its business operation or the status of its property, within the limit necessary.

(Emphasis added)

available to prohibit non-registered operators from carrying out illegal acts, there exist no effective means to suspend them other than an injunction issued by the courts. In addition, the number of general investors who acquired the shares of Seibutsu-Kagaku Research, Inc. as a result of the Defendants' illegal solicitation exceeded two hundred. The total amount paid by the investors was approximately 100 million yen and the Defendants earned more than 30 million yen from the fees without the requisite registration.

Accordingly, the Court held that it is necessary and appropriate to grant an injunction against the Defendants in light of public policy and protection of investors.

IV. Discussion & Analysis

1. Critique of Court Decisions: Requirements for Injunction

(1) Considered individually or comprehensively?

Deciding whether the requirements for issuing injunction under JFIEA § 192, the courts neither in the *Case of Daikyo, Inc.*⁴⁰ nor the *Case of Japan Realize, Inc.*⁴¹ discussed each requirement of “urgent necessity” and “necessary and appropriate for public interest and investor protection” individually, but concluded that these requirements were satisfied comprehensively.⁴² The court in the *Case of Japan Realize, Inc.*, without paying particular attention to the difference between “necessity” and “necessary” mentioned above, concluded that it was necessary and appropriate to prohibit the defendants from engaging in financial business without being registered in order to secure public interest and investor protection because administrative relief is not available against acts committed by non-registered financial business operators like the defendants, and injunction under JFIEA § 192 is the only effective relief available.⁴³

JFIEA § 192 (1), however, explicitly stipulates “necessity” and “necessary” separately.⁴⁴ Furthermore, “necessity” and “necessary” mean different requirements, as explained *infra* in

³⁹ JFIEA § 52, under the title of “Disposition rendered to a financial instruments business operator for the purpose of supervision,” provides as follows:

(1) In cases where a Financial Instruments Business Operator falls under any of the following items, the Prime Minister may *rescind its registration* under Article 29, *rescind its authorization* under Article 30(1), or *order suspension of all or part of its business* by specifying a period not exceeding six months:

...

(Emphasis added)

⁴⁰ See *supra* “III. First Decision to Grant an Injunction under JFIEA: *The Case of Daikyo, Inc.*”

⁴¹ For the *Case of Japan Realize, Inc.* (Sapporo District Court, May 13th, 2011), see <http://www.courts.go.jp/hanrei/pdf/20110613141003.pdf>.

⁴² Motokazu Endo, “Injunction under the Financial Instruments and Exchange Act—Recent Development and Practical Use of Injunction after the Revision of the Act,” 315 *Monthly Capital Market* vol. 25, 31 n.14 (2011).

⁴³ *Id.*

⁴⁴ For the text of JFIEA § 192, see *supra* note 1.

“IV. 1 (3) Meaning of ‘urgent necessity’ and ‘necessary and appropriate for the public interest and investor protection.’” Therefore, the decisions both in the *Case of Daikyo, Inc.* and the *Case of Japan Realize, Inc.* are not only contrary to textual interpretation, but are also misguided in that they confuse “necessity” with “necessary.” Whether the requirements of “necessity” and “necessary” are satisfied or not must be considered individually and separately, not comprehensively.

(2) A substitute to administrative relief?

By acknowledging the “non-availability of administrative relief,” the court in the *Case of Daikyo, Inc.*⁴⁵ held that the requirement of “urgent necessity” under JFIEA § 192 was satisfied. This decision is supported by a commentator.⁴⁶

However, the court’s interpretation of “urgent necessity” under JFIEA § 192 as “non-availability of administrative relief” is again clearly misguided. According to the court’s interpretation, an “urgent necessity” for an injunction would be considered to be lacking as long as the defendant is registered and administrative relief against the defendant is available. It is very easy to imagine a situation where a “registered” financial business operator continues to engage in an illegal act and keeps causing damage to so many investors that an injunction is strongly needed. Based on the decision in the *Case of Daikyo, Inc.*, however, a motion of injunction cannot be granted because the said financial business operator is “registered”⁴⁷ and “administrative relief” is available; “urgent necessity” for injunction is lacking.

Under the US securities regulations, from which JFIEA derives,⁴⁸ administrative relief, such as a cease-and-desist order, is not a substitute to an injunction order by the court.⁴⁹ An injunction is not something to be granted only if a cease-and-desist order is not available for investor protection.

Accordingly, “urgent necessity” should not be considered and interpreted as “non-availability of administrative relief.”

(3) Meaning of “urgent necessity” and “necessary and appropriate for the public interest and investor protection”

First, along its usual and textual meaning, if an injunction is urgent timewise, i.e., before an illegal act is completed, the requirement of “urgent necessity” under JFIEA § 192 can be judged to be satisfied because the injunction is designed to be a preventive measure against such illegal act causing damage to investors.⁵⁰ Second, even if an illegal act is completed, “urgent necessity” can still be satisfied because under JFIEA § 192, it is provided that “[a

⁴⁵ See *supra* “III. First Decision to Grant an Injunction under JFIEA: *The Case of Daikyo, Inc.*”

⁴⁶ Hidenori Hagiwara, “Active Use of Injunction under Financial Instruments and Exchange Act § 192,” 1923 *Shoji Houmu* 19, 20 (2011).

⁴⁷ Registered broker-dealers are now especially required to strictly comply with JFIEA since the Japanese Supreme Court decision in the derivative lawsuits against the directors of Nomura Securities Co. For detailed analysis of the said Supreme Court decision, See Hiroyuki Ogawa, “Case Note: Nomura Securities Derivative Lawsuit,” 126 *Hitotsubashi Review* 121 (2001).

⁴⁸ See *supra* “I. Introduction.”

⁴⁹ Etsuro Kuronuma, “Temporary Restraining Order against non-registered broker-dealers under Financial Instruments and Exchange Act § 192 (1),” 633 *Hanrei Hyouron* 43, 45-46 (2011).

⁵⁰ Kanda, Nomura Securities & Kawamura, *supra* note 8, at 1330-1331.

court] may give an order to a person who ‘has conducted’ . . . any act in violation of this Act.” Compared with the case when an illegal act is not completed, after it is completed, the court can judge more easily the likelihood of repeated occurrence of such illegal act in the future,⁵¹ and thus grant a motion of injunction.

In addition to “urgent necessity,” JSESC needs to prove that an injunction is “necessary and appropriate for public interest and investor protection.” One commentator argues that a motion of injunction is granted if an injunction is necessary and appropriate in light of “either” public interest “or” investor protection.⁵² This argument, however, is inconsistent with the text of JFIEA § 192, which explicitly states “public interest and investor protection.” Thus, this argument is unfounded and unsupportable.

Considering that JFIEA § 1 stipulates “fair price formation of Financial Instruments, . . . through the full utilization of functions of the capital market,”⁵³ along with “investor protection,” as one of JFIEA’s legislative purposes, the author construes “public interest” under JFIEA § 192 as “functions of the capital market.” Thus, if the court finds the defendant’s acts to be harmful to the “functions of the capital market,” one of the requirements is satisfied. For a motion of injunction to be granted, the court must also find that an injunction is necessary and appropriate for “investor protection,” which is not necessarily relevant to “functions of the capital market” but relates to private damages incurred by investors. A commentator proposes the following factors, i.e., the gravity of the illegal act, influence of the injunction if it is granted, and whether the defendant is conscious of committing an illegal act, as those to be considered in deciding whether the defendant’s act is harmful to investor protection.⁵⁴

Noting that the injunction under JFIEA originates in the US securities regulations, it will be found that the US case law, discussed in “2. (2)” above,⁵⁵ is greatly helpful and instructive for the Japanese courts in recognizing the crucial facts for public interest and investor protection and in deciding whether or not the granting of a motion of injunction is necessary and appropriate.

2. Injunction against Wrongful Acts Violating JFIEA § 157

JFIEA § 157, under the title of “Prohibition of wrongful acts”, stipulates as follows:

No person shall conduct the following acts:

- (i) to use *wrongful means*, schemes or techniques with regard to Sales and Purchase or Other Transactions of Securities or Derivative Transactions, . . . ;
- (ii) to acquire money or other property, using a document or other indication which contains false indication on important matters, or lacks indication about

⁵¹ See *supra* notes 25-27.

⁵² Kenichi Matsuo, *Commentary on Financial Instruments and Exchange Act* vol. 3, 476 (Masao Kishida ed., Kinyu Zaisei Jijyou Kenkyukai, 2010).

⁵³ For the text of JFIEA § 1, see *supra* “I. Introduction.”

⁵⁴ Makoto Oojita, “Injunction under Financial Instruments and Exchange Act § 192 —Case of *Daikyo, Inc.*”, 1367 *Kinyu-Shoji-Hanrei* 2, 5 (2011).

⁵⁵ To repeat the essential factors to be considered, they include (i) degree of scienter involved, (ii) sincerity of defendant’s assurances against future violations, (iii) the isolated or recurrent nature of the infraction, (iv) defendant’s recognition of the wrongful nature of his conduct, (v) likelihood that future violations might occur because of defendant’s professional occupation, (vi) gravity of the offense, and (vii) the adverse effect on the defendant.

important matters necessary for avoiding misunderstanding, with regard to Sales and Purchase or Other Transactions of Securities or Derivative Transactions, . . . ; or

- (iii) to use false quotations in order to induce Sales and Purchase or Other Transactions of Securities or Derivative Transactions, . . .
(Emphasis added)

The violator of JFIEA § 157 would be punished under JFIEA § 197 (1) (v).⁵⁶ Although JFIEA § 157 is deemed to be the most powerful deterrent against fraudulent acts, it has rarely been employed by the courts because some express a concern that excessive application of JFIEA § 157 may conflict with the principle of *nulla poena sine lege*, i.e., “no punishment without law.” This concern is not valid in my opinion.⁵⁷

From the perspective of investor protection, it is undeniable that an injunction is most needed in the situation where the perpetrator is trying to defraud the investor. A practitioner justifiably suggests that the court can grant a motion of injunction by finding that the defendant is attempting to defraud the investor, which act is punishable under JFIEA § 157.⁵⁸ The author agrees to his opinion under one condition: the court must find scienter, not negligence, of the defendant for defrauding the investor. This interpretation of JFIEA is in harmony with the US Supreme Court decision in *Aaron v. SEC*;⁵⁹ the US Securities and Exchange Act § 10 (b) and Securities Act § 20 (b) are the model codes for JFIEA § 157 and JFIEA § 192, respectively.

3. Rescission or Change of Injunction under JFIEA § 192 (2)

Some may fear that granting a motion of injunction based on JFIEA § 157 would have a chilling effect on securities transactions. This adverse effect, however, can be avoided or minimized if the court promptly and liberally rescinds or changes the decision of injunction.

JFIEA § 192 (2) provides that “[the] court may rescind or change the order issued under JFIEA § 192 (1).” JFIEA § 192 (4), then, provides that “[t]he judicial decision under JFIEA § 192 (1) and (2) shall be governed by the Non-Contentious Cases Procedure Act (‘NCCPA’).” NCCPA § 19 (1) provides that “[t]he court can rescind or change the judgment if the court later finds the judgment to be unfair,” but NCCPA does not provide for the standing to rescind or change the judgment. Therefore, the court can voluntarily rescind or change the injunction

⁵⁶ JFIEA § 197 (1) provides in a pertinent part as follows:

- (1) Any person who falls under any of the following items shall be punished by imprisonment with work for not more than ten years or by a fine of not more than ten million yen, or both. . . .
- (v) a person who has violated *the provisions of Article 157, Article 158, or Article 159.*

...

(Emphasis added)

⁵⁷ Hiroyuki Ogawa, “Definition of ‘Business of Insurance,’ Legislative Purpose of and Public Interest Implied in the Insurance Business Act: Comparative Analysis with Banking and Securities Regulation,” 177 *Japan Institute of Life Insurance Journal* 89, 94-95, 104, n. 25 (2011).

⁵⁸ Satoru Nakamura, “Several Issues for Investor Protection concerning Equity of Investment Scheme,” in *Modern Subjects about Financial Instruments and Exchange Act* 102, 124 (Japan Securities Research Institute, 2010).

⁵⁹ 446 U.S. 680 (1980). See also *supra* “II. 2 U.S. Securities Act § 20 (b)” for further discussion on the requirements for granting a motion of injunction.

without a motion from the parties.⁶⁰

Under what circumstances, then, can the court later rescind or change an injunction? You can find neither precedents nor an explicit code with respect to the requirements for rescission or change of an injunction. In this respect, the US case law offers valuable guidance again. Based on the decision in *SEC v. Warren*, the court can dissolve and modify an injunction if the hardship brought to the defendant by prospective application of the injunction outweighs the necessity to continue the injunction and the severity of the alleged danger which the injunction was originally designed to eliminate.⁶¹ Thus, the Japanese courts, after weighing several factors mentioned in the decision of *SEC v. Warren*, can rescind or change an injunction if they find the continuation of the injunction to be unfair pursuant to NCCPA § 19 (1).

4. Revision of JFIEA § 187: Supplemental Measure to Injunction

Injunction under JFIEA § 192 is supplied with effectiveness by the power to investigate under JFIEA § 187, which provides as follows:

The Prime Minister or the Prime Minister and Minister of Finance may have the officials take *the measures* listed in the following *for the purpose of conducting investigation necessary . . . for a petition under the provisions of Article 192*:

- (i) to order a person concerned or a witness to appear so as to hear his/her opinions, or to have said person submit a written opinion or a written report;
- (ii) to order an expert witness to appear so as to have him/her present an expert opinion;
- (iii) to order a person concerned to submit books and documents or other articles, or to retain the submitted articles; and
- (iv) to inspect the status of business or property, or the books and documents or other articles of a person concerned.

(Emphasis added)

The US counterpart of JFIEA § 187 is the Securities and Exchange Act § 21 (a), which provides, under the title of “Authority and discretion of Commission to investigate violations” as follows:

(1) *The [Securities and Exchange] Commission* may, in its discretion, make such investigations as it deems necessary to determine whether any person has violated, is violating, or is about to violate any provision of this chapter, the rules or regulations thereunder, . . . and *may require or permit any person to file with it a statement in writing*, under oath or otherwise as the [Securities and Exchange] Commission shall determine, as to all the facts and circumstances concerning the matter to be investigated. *The [Securities and Exchange] Commission is authorized in its discretion, to publish information concerning any such violations*, and to investigate any facts, conditions, practices, or matters which it may deem necessary or proper to aid in the enforcement of such provisions, in the prescribing of rules

⁶⁰ Kanda, Nomura Securities & Kawamura, *supra* note 8, at 1333.

⁶¹ See *supra* note 33.

and regulations under this chapter, or in securing information to serve as a basis for recommending further legislation concerning the matters to which this chapter relates.

(Emphasis added)

This investigative power of SEC functions as a negotiating tool. The report pursuant to the Securities and Exchange Act § 21 (a) can be used as a substitute for administrative disciplinary or civil injunctive suits in marginal and less egregious cases, having sometimes the effect of inducing subject parties to settle.⁶²

The ultimate goal of the injunction under the Japanese and the US securities regulation is investor protection by prohibiting illegal and wrongful acts. JFIEA § 187, however, does not give JSESC the power to “require . . . any person to file . . . a statement in writing, under oath” and the power “to publish information concerning any . . . violations,” both of which the Securities and Exchange Act § 21 (a) does give to SEC. It is obviously desirable from the viewpoint of investor protection that JSESC be furnished with both of the said powers by way of revising JFIEA § 187. Once this revision of JFIEA § 187 is made, JSESC does not always have to resort to injunction under JFIEA § 192, but can persuade the (prospective) defendants into stopping illegal and wrongful acts by making the most of the powers given under the revised JFIEA § 187. If JSESC files fewer motions of injunction, court resources would be saved.

5. Disgorgement

A commentator doubts the effectiveness of the injunction because the Japanese courts cannot order defendants to disgorge the illegal profits gained by their wrongful acts.⁶³ Another commentator argues that injunction is mostly used for the purpose of disgorgement in US.⁶⁴

The Japanese government admits that the court cannot collect money by issuing injunction, and it expresses the need to introduce a new legal framework for the relief of investors, by which the court can force a perpetrator to disgorge illegal profits.⁶⁵

In US, collective relief for damaged investors is attainable through “Fair Funds.” When disgorgement and a civil money penalty are ordered against a perpetrator in an enforcement action, SEC is authorized by the Sarbanes-Oxley Act of 2002 to establish a fund for the benefit of investors that would help offset their losses incurred by illegal acts committed.⁶⁶ Injunction under JFIEA § 192, if combined with a remedy similar to Fair Funds, is expected to be more efficient and effective for investor protection because damaged investors can take back the money from the perpetrator through the disgorgement procedure.

⁶² Steinberg, *supra* note 32, at 416.

⁶³ Yamashita & Kanda, *supra* note 18, at 456.

⁶⁴ Etusro Kuronuma, “Enforcement for Investor Protection,” 1907 *Shoji Houmu* 43, 48 (2010).

⁶⁵ The Japanese Cabinet Office, Bureau of People’s Lives, “Report on the Institution for the Collective Relief for Consumers (August 2009),”

<http://www.caa.go.jp/planning/pdf/torimatome.pdf> at 13-14.

⁶⁶ *SEC v. Genstar TV Guide International*, 367 F.3d 1087, 1090-91 (9th Cir., 2004); Steinberg, *supra* note 32, at 157.

V. *Concluding Caveat*

JSESC has lately been given the power to initiate injunction procedures by the repeated revisions of JFIEA.⁶⁷ Against the backdrop of this recent enhancement of the power of JSESC, it may be culpable for not exercising its authority to secure investor protection.⁶⁸ The court in the *Case of Daiwa Toshi Kanzai* notes that “non-exercise of the authority can be deemed illegal pursuant to the Japanese State Redress Act (“JSRA”) § 1 (1)⁶⁹ when the nonfeasance, in light of the legislative purpose and the nature of the authority, is extremely unreasonable under the given circumstances.”⁷⁰

Furthermore, the Japanese government declares the following in the “Fundamental Plan for Consumer Protection: Decision of the Cabinet Office (2010)”⁷¹:

As cases arise where non-registered financial business operators engage in offering non-registered securities⁷² and in fraudulent transactions,⁷³ the draft to revise JFIEA, which includes more severe punishment, must be submitted to the Diet,⁷⁴ and further discussion must be held among officials concerned after the said revision of JFIEA.

(Footnotes supplied)

In conclusion, the members of the legislative, administrative, and judicial branches must now work much harder in pursuit of ensuring investor protection.

⁶⁷ See *supra* “II. 1 JFIEA § 192.”

⁶⁸ Yasuhito Oomori, “Injunction,” 1914 *Kinyu-Houmu-Jijyou* 19, 26 (2011) .

⁶⁹ JSRA § 1 (1) provides as follows:

When a public officer who *exercises the public authority* of the State or of a public entity has, in the course of his/her duties, unlawfully inflicted damaged on another person intentionally or negligently, the State or public entity shall assume the responsibility to compensate therefor.

(Emphasis added)

⁷⁰ Osaka District Court (second civil branch), June 6th, 2007.

⁷¹ <http://www.caa.go.jp/planning/pdf/100330keikaku.pdf>.

⁷² See the *Case of Daikyo*, *supra* “III. First Decision to Grant an Injunction under JFIEA: *Case of Daikyo, Inc.*”

⁷³ See the *Case of Japan Realize, Inc.*, *supra* “IV. 1 (1) Considered individually or comprehensively?”

⁷⁴ The draft has been enacted. See *supra* “II. 1 JFIEA § 192.”