

Subsidy Program for Domestic Site Location
(Second Public Offering)
(Provisional translation)

**Ministry of Economy, Trade and Industry
Economic and Industrial Policy Bureau,
Economic and Industrial Policy Division
April 2012**

I. “Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake” from the Reconstruction Headquarters in response to the Great East Japan Earthquake (July 29, 2011)

5. Reconstruction measures

(3) Revitalization of regional economic activity

(i) Corporations, industrial technology, etc.

- Provide measures to encourage companies to locate their production bases domestically, and improve the location environment for companies in Japan, in order to avoid the possibility that the disaster may have triggered acceleration of “hollowing out” of its industries by companies moving to relocate their production bases from Japan to other countries. These measures will be offered for production bases and R&D sites in the fields of parts and materials, which constitute the core part of the supply chain and cannot be substituted, as well as high added value growth sectors, which will create employment in our country.

II. “Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake” from the Democratic Party of Japan (July 29, 2011)

2. Economic policy to reconstruct Japan (Nationwide programs)

(1) Measures against hollowing out of industries

- Provide measures to encourage companies to locate their production bases domestically and improve the location environment for companies in Japan. These measures will be offered for production bases and R&D sites in the fields of parts and materials, which constitute the core part of the supply chain and cannot be substituted, as well as high added value growth sectors, which will create employment in our country.

III. Recommendations from the Great East Japan Earthquake Reconstruction Design Council (June 25, 2011)

(5) Revival of Local Economic Activities

(i) Private companies and innovation

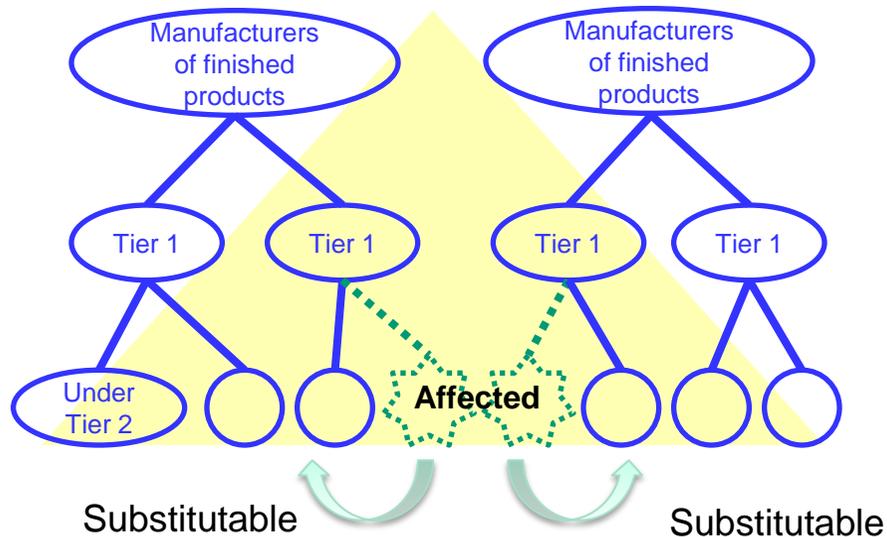
- Provide measures to promote site location, such as supporting the revival of the supply chain, and improve the location environment for companies in Japan.

- Manufacturers of finished products assume a “Pyramidal structure,” where business partners procure parts and materials from several suppliers at each tier and ensure substitutability.
- However, in reality, the supply of materials is concentrated among a few “under tier 2” suppliers and substitutability is not ensured. (“Diamond structure”)

【Assumption】

Pyramidal structure

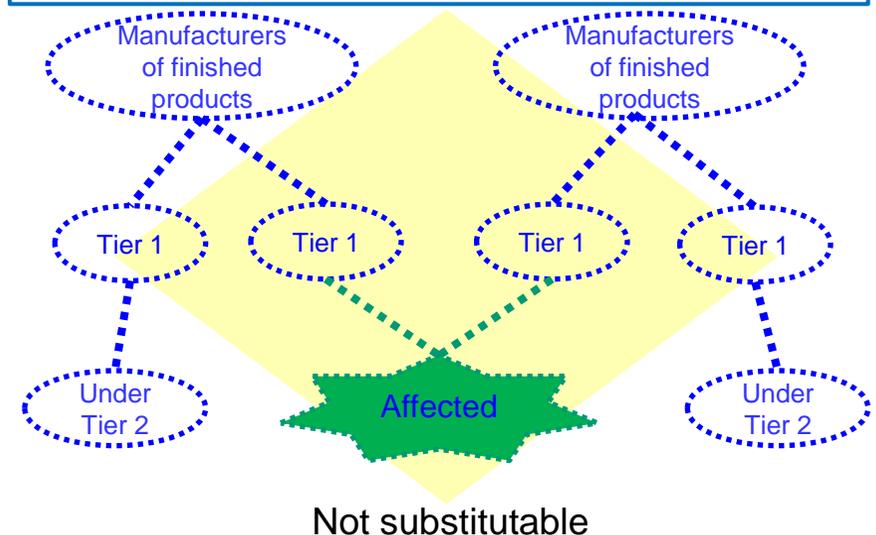
- Multiple parts and materials manufacturers at each tier form a pyramidal structure
- Suppliers are substitutable at both upper and lower tiers



【Reality】

Diamond structure

- Some parts and materials are concentrated among a few limited suppliers
- Since these suppliers have been affected by the earthquake, the whole supply chain has been affected



➤ Since the earthquake, lobbying of Japanese corporations in core sectors, which are expected to grow in the future, by foreign governments has been intensified

- **Survey Question Asked: Since the earthquake, have you ever been invited to relocate overseas by foreign governments or companies? Or have the invitations been intensified?**



- **11 corporations out of 161 answered “Yes” or “Intensified.”**
 - **Companies or countries that attracted the 11 corporations above are as follows:**
 - 4 companies were invited to China, 2 to Korea, and one each to Singapore, Thailand, Malaysia, the USA, and Canada**
- (Note) Not all of the corporations gave the names of the countries or companies that invited them.

(Ref.) “Survey of Revival and Hollowing-out of Supply Chain Since the Great East Japan Earthquake” by METI

【Lobbying by foreign governments】

City A, South Korea	Dispatched a group to attract Japanese corporations in May; plans to exempt corporate tax for 3 years and income tax for 7 years.
City B, South Korea	Plans to offer individual consultations, with the Korea Trade-Investment Promotion Agency (KOTRA) serving as an intermediary. Continues to attract Japanese corporations, including establishment of joint corporations.
City C, China	(Through visits to Japanese corporations to express sympathy after the earthquake) “We realized that Japanese corporations plan to accelerate industrial transformation. This is a good opportunity for us to attract Japanese corporations. We would like to emphasize that we are better than other cities in terms of transportation, hydro-electric generation, human resources, and technologies.”

Industrial fields that foreign governments are competing to acquire



Solar panels



Electric vehicles



Lithium-ion batteries

- Concern over the disruption of the international supply chain has increased. To take the lead in next-generation industry, competition among foreign countries to acquire technologies with a central focus on parts and materials has intensified.



- **Worked out “comprehensive measures to increase the competitiveness of its domestic parts and materials manufacturers”**

- 1) The government plans to invest **R&D worth 1 trillion won (approx. 80 billion yen)** to develop 10 globally competitive industrial materials by 2018.
- 2) A **300-billion-won parts and materials fund** was raised by the Korea Development Bank with an aim to acquire foreign parts and materials corporations.

The 10 World Premier Materials (WPM)

1. Environment-friendly Smart Surface Treated Steel Plates (POSCO)
2. Ultra-lightweight Magnesium Materials for Transport Planes (POSCO)
3. Energy-efficient Multi-function Nano Compound Materials (LG Chem Ltd.)
4. Multi-function Macromolecular Membrane Materials (Kolon Fashion Material)
5. Plastic Substrate Materials for Flexible Displays (Cheil Industries)
6. Electrode Materials for High Energy Secondary Batteries (Samsung SDI Co.)
7. Bio Medical Materials (AminoLogics)
8. Ultra-pure Silicon Carbon (SiC) Material (LG Innotek Co.)
9. Sapphire Single Crystal Materials for LEDs (Sapphire Technology)
10. Carbon Reducing-type Ketone Premium Textiles (Hyosung)



- The government identified next-generation vehicles as a strategic field and **formed a “national team” to develop the industry for parts that are critical to electric vehicles.**
- BYD, a Chinese car manufacturer, announced plans to export new-energy cars such as **electric vehicles (EV), starting from October to December 2012.** (March 2011)

2. Massive expansion of site location subsidies

1. Provide site location subsidies totaling 140 billion yen (29.7 billion yen from the supplementary budget of FY 2009 and 110 billion yen from contingency funds of FY 2010) for low-carbon industries such as lithium-ion batteries, LEDs, and eco-friendly cars, to build a new or additional factory with an aim to deal with the international competition for site location following the Lehman Shock. (Note) The original fiscal 2011 budget allotted 7.1 billion yen for subsidies.

 Induce investment of 670 billion yen, five times as much as subsidies, and create derived demand of 2.2 trillion yen and 112,000 jobs

3. Since the earthquake, outflow of domestic industries to foreign countries owing to **the appreciation of the yen, power constraints**, and the hollowing out of domestic industries and employment, has raised the fear that not only the regional economy but also the national economy will be damaged. Therefore, **site location subsidies will be drastically expanded in the third supplementary budget for not only the affected areas but also nationwide**. Specifically, capital investment to corporations of not only the low-carbon industry but also the following industries will be subsidized (*):
 - i. **Parts and materials industries** (crystal devices, rare earth magnets, electrolytic membranes for batteries, special microcomputers, and LED components)
 - ii. **Growth industries** (highly functional liquid crystal panels, lithium-ion batteries, and wind power generation)

* Subsidy rate: 1/3 in principle, 1/2 for small and medium enterprises (2/3 for small and medium enterprises in a group)

- (Ref.) Policy Speech by Prime Minister Yoshihiko Noda (excerpt)
(Implementation of drastic countermeasures against the appreciation of the yen and the hollowing out of industries)
- We will implement emergency economic measures such as drastically **expanded subsidies for site location** by means of contingency funds and the third supplementary budget.

Objectives

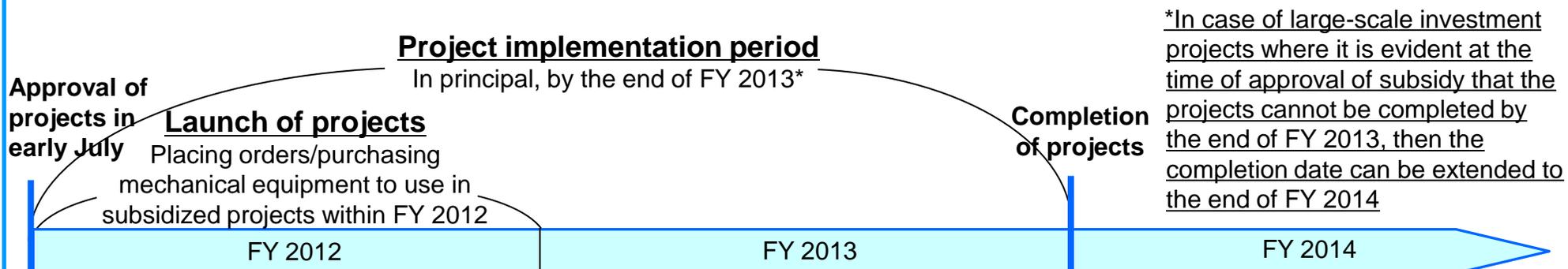
This subsidy program is an implementation of the policy based on the Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake and the basic principles stipulated in Article 2 of the Basic Act for Reconstruction in Response to the Great East Japan Earthquake, with the purpose of facilitating reconstruction in the aftermath of the Great East Japan Earthquake. The program aims to improve the logistics and facilities of the business locations of companies operating within Japan as well as encourage new investment to maintain and create employment by providing domestic site location subsidies to the production sites in the fields of parts and materials that constitute the core part of the supply chain and cannot be substituted; and high added value growth sectors, which will sustain future employment in our country.

Description

Budget: 295 billion yen [Of which approx 202.3 billion yen was approved on February 3]
 Subjects: Private enterprises
 Subsidy rate: 1/3 or less in principle
 1/2 or less for small and medium enterprises
 2/3 or less for small and medium enterprises in a group

Maximum limit of subsidies: 15 billion yen

Eligible subjects: As described below (Expenses for mechanical equipment used in enterprises' production facilities)
 (Note) Excludes projects whose specific investment plans, such as construction and completion schedules, were announced prior to the release of the Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake on July 29.



Subsidy requirements A (must meet (i) and (ii) below)

- A. The fields of parts and materials, which constitute the core part of the supply chain and cannot be substituted
- (i) The fields of parts and materials, which constitute the core part of the supply chain and cannot be substituted (must meet both a and b below)
 - a. Must hold a domestic share of more than 10%
Or
Business partners demand that the applicant company invest in the field to improve the supply system by means of decentralization or dualization.
 - b. Must have a low import substitution (percentage of imports must be low)
 - (ii) The applicant company must maintain a level of domestic employment in the sector-specific departments qualified under the subsidy, equal to the pre-earthquake standard, for 4 years.
(However, small and medium enterprises in a group or based in an affected area may maintain a level of employment in the entire manufacturing facility qualified under the subsidy, equal to the pre-earthquake standard, for 4 years.)

(Note) The business operators must report on the achievement of employment levels every year as well as their compliance with labor laws.

Subsidy requirements B (must meet (i)–(iii) below)

B. High-added-value growth sectors that create employment

(i) Manufacture of products or parts related to the field that is expected to have growth potential (must meet both a and b below)

a. Fields referred to in government documents such as:

- Fields of “green innovation” or “life innovation” in “New growth strategy” (Cabinet approval in June 2010)
- Strategic growth fields (Ref.) in “Industrial Structure Vision 2010” (announced in June 2010 by METI)
- “Cool Earth - Innovative Energy Technology Program” (announced in March 2008 by METI) (Ref.)
- “Innovation Plan for Environmental Energy Technology” (announced in May 2008 by the Council for Science and Technology Policy) (Ref.)

b. Fields expected to have high growth potential

Those in which the market size has expanded more than 25% in the most recent 2 years (from 2008 to 2010)

(Note) The final assembly process of products cannot solely be eligible for the subsidy, in principle. However, in the case where the introduction of innovative manufacturing processes increases the added value (if one of the following improves more than 20%: an assembly line’s total asset efficiency, energy efficiency, or labor productivity), the final assembly process itself may be eligible for the subsidy.

(ii) Drastic investment that will lead to new market creation/expansion

(This requirement is an additional point for private limited companies or small and medium -sized enterprises).

The subsidized business will invest more than that which the current account balance allows for general investment (*), or

The subsidized business will invest more than 5 billion yen

(*) That which the current account balance allows for general investment = (cash and deposits on B/S - short-term debt) – (average sales per month) x 2.4

(iii) Creation of stable and lasting domestic employment

Create jobs of more than 3 person-years (*) per subsidized costs of 100 million yen in principle

(*) For example, if the subsidized cost is 400 million yen and the company makes a long-term hiring commitment of 4 years, then jobs should be created for more than 12 persons (more than 3 persons x 4 years). The shortest term should be 4 years (more than 3 persons x 4 years), while the longest term should be 10 years (more than 1.2 persons x 10 years). *where the subsidized cost is 400 million yen

However, if (1) the investment will be made in affected areas, (2) the additional value of the final assembly process will be increased by introduction of an innovative production process (if one of the following improves more than 20%: an assembly line’s total asset efficiency, energy efficiency, or labor productivity), or (3) the subject is a small or medium enterprise in a group, the requirement will be to maintain a level of domestic employment in the departments qualified under the subsidy, equal to the pre-earthquake standard.

(Note) The business operators must report on the achievement of employment levels every year as well as their compliance with labor laws.

Strategic industrial fields in “Industrial Structure Vision 2010” (announced in June 2010 by METI)
(<http://www.meti.go.jp/committee/materials2/downloadfiles/g100601a05j.pdf>)

Strategic industrial fields

- I. Asian industries with high income elasticity
- II. Fields with high carbon productivity
- III. Fields with expanding markets due to an aging society and a declining birthrate

- (1) Infrastructure-related/system export (nuclear power, water, railways, etc.)
- (2) Industries that solve environmental/energy problems (smart community, next-generation vehicles, etc)
- (3) Culture business (fashion, content, food, tourism, etc.)
- (4) Medical, nursing-care, health, and child-rearing services
- (5) Advanced areas (robots, space, etc.)

“New Growth Strategy: Blueprint for Revitalizing Japan” (Cabinet approval in June 2010)
(http://www.npu.go.jp/policy/policy04/pdf/04/06/20100618_shinseityousenryaku_honbun.pdf)

“Problem-solving” national strategy

The New Growth Strategy has identified growth areas as “green innovation,” “life innovation,” “the Asian economy,” and “tourism and regions.” The government will implement strategies related to “science and technology and information and communications technology,” “employment and human resources,” and the “financial sector,” which are areas essential to supporting growth.

- (1) Green innovation (storage batteries, next-generation vehicles and lighting, etc.)
- (2) Life innovation (medical equipment, medical/nursing-care robots, etc.)

Cool Earth - Innovative Energy Technology Program (2008 Ministry of Economy, Trade and Industry)

“21” innovative energy technologies to be prioritized

- (1) Power generation/transmission (innovative photovoltaic power generation, etc.)
- (2) Transportation (fuel cell vehicles, plug-in hybrid vehicles, electric vehicles, etc.)
- (3) Industry (innovative iron and steel making processes, etc.)
- (4) Commercial/residential (next-generation high-efficiency lighting, stationary fuel cells, etc.)
- (5) Cross-cutting technologies (high-performance power storage, power electronics, etc.)

“Innovation Plan for Environmental Energy Technology”

(May 2008, Council for Science and Technology Policy)

Our national technology strategy towards realizing a low-carbon society

- (1) Technology that leads to large-scale reductions (high-efficiency heat pumps, energy-saving household electrical appliances/information technology devices, etc.)
- (2) Technology to reduce greenhouse gas at region-wide level (high-efficiency railway vehicles, biomass, etc.)
- (3) Combining technologies that further reduce emissions of greenhouse gas (sustainable energy (photovoltaic generation/wind generation) and power storage (rechargeable batteries/capacitors), etc.)

Requirements for small and medium enterprises in a group

- (i) Be part of a joint business formed by several other small and medium enterprises
- (ii) Meet subsidy requirements A or B
- (iii) Utilize the core technologies (*) as a group to manufacture important or high added value products in the supply chain. With the aim of making their business more consolidated, efficient and strong, to cope with the strong yen and overcome fierce international competition, the group must have one of the following merits of grouping:
 - (1) Advantage of scale (efficiency achieved by scale expansion)
e.g., improvement of factory-operating ratio or reduction of procurement cost with a larger order quantity of materials
 - (2) Synergy effect (effect brought about by complementing technologies)
e.g., improvement of flexibility of development and manufacturing due to the increase of technologies, supply sources, and buyers

* Core technologies here include forging, cutting, and heat treatment for small and medium enterprises.

5. Important criteria in screening

Applicant companies are screened in terms of the criteria below, as well as basic criteria such as fiscal health and implementation systems for the subsidy projects.

A. Competitiveness/Low-substitutability

Competitiveness: Is it expected to ensure sufficient shares in the target growing market?

Low-substitutability: Does the product or technology have low substitutability? (e.g., it commands more than half of the domestic market share)

B. Sufficient investment scale

Is the investment large enough compared to the future market scale, or large enough to compete with other companies? Is the investment large enough compared to the scale of the applicant company? Is the subsidy project the only way to get the sufficient investment?

C. Business collaboration

Can the business work in collaboration with companies in the same industries as well as upstream/downstream companies, in view of future restructuring or specialization to improve efficiency in order to maintain and improve competitiveness?

D. Concern over international relocation

Is there any concern over international relocation due to the appreciation of the yen? Are any foreign governments interested in attracting manufacturers of the same type of products, parts, or materials? Do those governments offer any site location subsidies?

E. Decentralization/Dualization

Does the business aim at decentralization or dualization to deal with the aftermath of the Great East Japan Earthquake?

F. Establishment of a business continuity plan (BCP)

Has the applicant company established a BCP to manage potential risk and fulfill its responsibility as a supplier?

G. Job creation

Will the business create stable and lasting domestic employment? Will the business create employment in the related industry?

H. Technology

Do the products, parts, or materials utilize innovative technology? Does the applicant company have reliably safe technology? Is the technology commercially successful enough to have many (potential) buyers?

I. Cluster effect/Regional partnership

Will the business have a positive ripple effect on the regional economy and industry? Is it associated with existing measures for regional revitalization?

6. Key changes from first public offering

1. Review and clarification of operating procedures

<Clarification of application process in case of joint application> *The operating procedure is clearly stated in the guideline of the first public offering

(Joint application for Requirements A and B)

Applications for Requirements A and B should in principal be applied for by a sole applicant company; however, if the business will not be formed by a sole applicant company (as shown in examples below), a joint application by several companies will be accepted.

(Examples)

- When the equipment investment function, production planning function, and production function are dispersed among different companies.
(When the production function is commissioned to subsidiary company)

- In cases where a leasing company is used (see below)

In the case of a joint application, please be aware that extra application forms will need to be submitted.

<Addition in application by syndicated lease>

One company should act as the administrative agent to represent the rest and deal solely with all administrative procedures. In some cases, where the refund obligation for the subsidy is borne by the administrative company, a joint lease system may be permitted.

<Addition of disqualifying conditions and attachment of list of officers>

Disqualifying conditions

(i) A person who is subject to an order prohibiting them from receiving subsidies or an order disqualifying them from bidding for projects conducted under the “designated bidder” system by the Ministry of Economy, Trade and Industry (METI)

(ii) A business operator to which the following applies

1. When the owner of the business or, where the owner is a corporation, the officers of that corporation or people who are responsible for supervising the business or their equivalent (referred as “officers, etc.,” hereinafter) are members of an organized crime group or people controlled by members of an organized crime group (as prescribed in Article 2, item (vi), of the Act on Prevention of Unjust Acts by Organized Crime Group Members (Act No. 77 of 1991, referred to as the “Anti-Organized Crime Law” hereinafter), with this same definition applying hereinafter).

2- 8 (omitted)

<Sufficient level of investment>

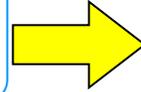
A sufficient level of investment will be an additional point for private companies and small and medium-sized enterprises.

2. Clarification of prescribed points

“Requirement A”

<Low-substitutability/competitiveness>

Whether its low-substitutability can be maintained in the future (or explanation of level of its low-substitutability)
(Additional point)



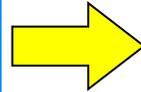
3. Explanation of present and future low-substitutability (additional point)

- State in detail if the originality and specialty (high technology, etc.) of said parts/material compared with the products of competitors (including overseas) can be maintained.
- State in detail if low-substitutability will be maintained in the future

“Requirement B”

<Impact on employment>

(Note 1)
Consider the first fiscal year of fulfilling the employment requirement as (N) and state the last year of fulfilling the employment requirement as (α)
(2 yrs) ≤ 「α」 ≤ 10 (yrs)



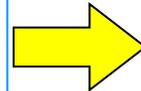
(Note 1) Consider the first year of business with equipment installed for the subsidized business as (N) and state the year (α) until it becomes ≥ 3 people/year/hundred million
(4 yrs) ≤ 「α」 ≤ 10 (yrs)

- * It is permissible to state the employment plan for the subsidized business even after fulfilling the employment requirement (after α)
However, be aware that during the period stated above, there will be an obligation to issue an employment report. (In this case, the upper limit for stating will be the 10th year starting in N fiscal year.)

“Common requirements for A to C”

<Business collaboration>

1. Effects of business collaboration with other companies in the same industry
* State in detail the effects, etc., of collaboration with other companies in the same industry, such as business collaboration in view of future restructuring and specialization to improve efficiency. Attach any documentation of the contents of agreed collaboration.



1. What challenges there are to maintain and improve competitiveness in the subsidized business fields and what kind of business collaboration with upstream/downstream companies (business cooperation, M&A, etc.) are encouraged or under review to deal with the challenges.

- State only business collaboration related to the project
- Attach documentation, if any, regarding the contents of agreed collaboration.

2. Specifically, in what form can maintaining and improving competitiveness be achieved for the business through the above business collaboration.

 - Focus on stating why the business cannot be realized by a sole company but can be delivered through business collaboration

FY 2012

April 6

Opening of the second public offering of the subsidy

During April

Briefing session

(Bureaus of Economy, Trade and Industry/Regional Bureaus, etc.)

June 1

Closing of the second public offering of the subsidy

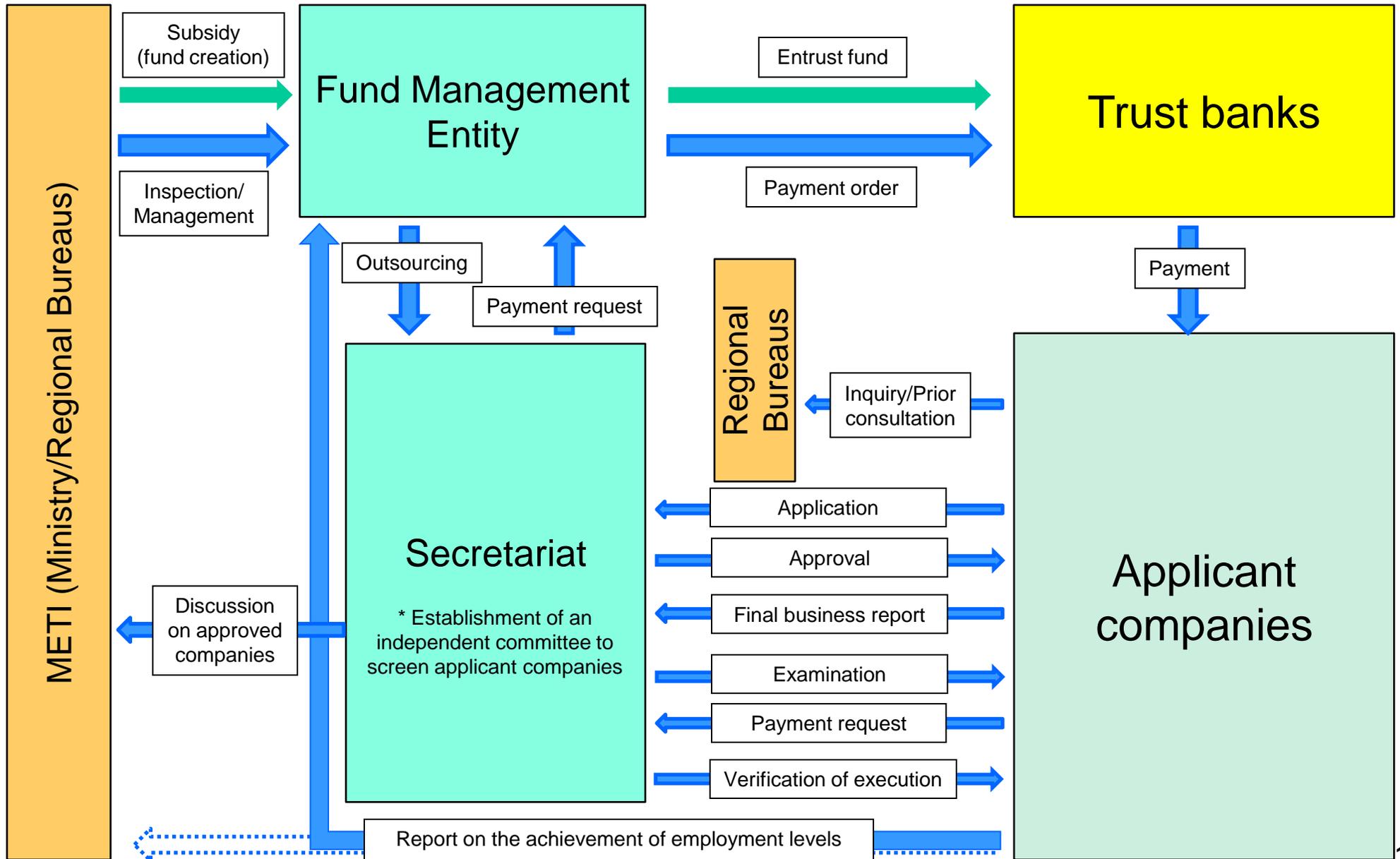
During June

Screening by a third-party committee

Early to Mid-July

Approval of projects

8. Subsidy scheme



Background

- It is clearly stated in the “Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake” prepared on July 29, 2011, that “due to the earthquake...acceleration in the hollowing out of industry in the affected area is feared...support will be offered for production bases and R&D centers locating within Japan” and 295 billion yen has been allocated from the third supplementary budget of FY 2011.
 - On the basis of the “Basic Guidelines for Reconstruction in Response to the Great East Japan Earthquake,” a public offering was announced for the fields below:
 - A. The fields of parts and materials that constitute the core part of the supply chain and cannot be substituted;
 - B. High-added-value growth sectors that create employment; and
 - C. Groups of small and medium-sized enterprises, etc., who operate in A or B.
- There was an enormous response from across the country, with the number of applicants far exceeding the planned budget.

Results

- Number of applicant companies: 748
(of which 358 were small and medium-sized enterprises)
- Number of approved companies: 245
(of which 81 were small and medium-sized enterprises)
- Total cost of subsidies: approx. 202.3 billion yen
- Method of approval
Screening by a third-party committee on the basis of impacts on employment creation, risk of technology moving overseas, contribution to a strengthened supply chain, competitiveness, strength of technology, and subsequent impact on local economy.
- Schedule
November 21 (Mon) Third supplementary budget passed
November 29 (Tue) Opening of first public offering
Screening committee met twice in each of the 3 fields
January 29 (Sun) Final approval by General Coordination Committee
February 3 (Fri) Announcement of approved projects



Expected effects in future

Economic effects

- Inducing capital investment of **1.26 trillion yen, about 6 times** the actual subsidy cost
- Creating demand of approx. **4.9 trillion yen** annually in supporting industries

Job creation effects

- Creating **approx. 200,000 jobs** including in supporting industries