
LAWS AND REGULATIONS

This section sets forth a summary of the most significant aspects of Japanese laws and regulations relating to our business in Japan.

GENERAL OVERVIEW OF THE JAPANESE LEGAL SYSTEM

Primary Features

The Japanese legal system has the following significant features:

- The Japanese legal system is a hybrid civil law system with characteristics of both civil law systems, such as the French and German civil legal systems, as well as common law systems, such as the United States legal system.
- Under Japanese law, any act, including our operations under the Three Party System, shall not be subject to criminal prosecution unless such act is explicitly and clearly described as a crime under a strict contextual interpretation of the applicable statutory provisions.
- Court rulings, although they have a *de facto* binding effect on inferior courts, do not modify existing law or create new law. Laws can only be adopted or modified through the legislative process.
- Court rulings, similar to court rulings in other civil and common law systems elsewhere, may be overturned by laws and regulations and/or amendments to existing laws and regulations enacted or adopted by legislative or executive authorities.
- The highest court in Japan is the Supreme Court.

Historical Background

The early modernisation of the Japanese legal system in the mid-19th century to early-20th century was primarily influenced by the German and French codes, which are civil law codes that served as models for the major Japanese codes such as the Civil Code.

After the Second World War, some laws in Japan such as the Constitution of Japan (the “Constitution”), criminal procedure laws, and labour laws were amended or replaced using principles from United States law, which is based on the common law. Therefore, the Japanese legal system is a hybrid of the civil law system and the common law system, and has evolved substantially independently in accordance with the Japanese legal culture.

The distinction between common law and civil law mainly lies in the precedential value of case law. In a common law legal system, judicial decisions of superior courts have precedential value in later court decisions and form part of the common law, along with laws and regulations enacted or adopted by the legislative and executive branches of government. As a result, judges in a common law system have a substantial role in shaping the law.

In contrast, a civil law system tends to be a codified body of broad and general principles. The judge’s role is to establish the facts of the case and to apply the provisions of the applicable code. Judicial decisions are consequently less crucial in the development of the law.

Generally, the Japanese legal system operates to proscribe unacceptable conduct, rather than prescribe particular types of permissible conduct. In other words, under Japanese law, conduct is generally allowed unless it is stated as prohibited under the law.

LAWS AND REGULATIONS

Constitution

Japan's current legal system was established by the Constitution, promulgated on 3 November 1946 after the Second World War. The Constitution provides for the separation of the legislative, judicial and executive powers.

The Constitution establishes a parliamentary system of government, where the legislative authority is vested in a bicameral National Diet (the "Diet"); the executive authority is exercised by the Prime Minister and the cabinet who are answerable to the legislature; and the judiciary is headed by the Supreme Court of Japan.

Source of Law and Legislative Process

The sources of Japanese law include the Constitution, Treaties and International Agreements, Acts, Cabinet Orders, Ministry Ordinances and Ministry Notifications.

Under Article 98 of the Constitution, the Constitution is the supreme law of the nation and no law, ordinance, imperial rescript or other act of government, or part thereof, contrary to the provisions hereof, shall have legal force or validity.

Under Article 41 of the Constitution, the Diet is the highest organ of state power and the sole law-making body. The Diet is made up of two houses, the House of Representatives (*Shugi-in*) and the House of Councillors (*Sangi-in*). Under the Japanese legislative process, most draft bills come from the executive and are then submitted to the Diet through the Cabinet. To become law, a bill must pass both houses of the Diet. Japanese law comprises written laws that fit into a certain hierarchy, headed by the Constitution. Statutes are often sorted, by subject matter, into substantive and procedural laws. The Cabinet and each Ministry may make subordinate regulations such as Cabinet Orders, Ministry Ordinances and Ministry Notifications based upon delegation from the Diet.

Judiciary

Under the Constitution, the Supreme Court is the highest court in the nation exercising appellate jurisdiction. The high courts are appellate courts primarily hearing appeals from district courts or family courts. The district courts are primarily courts of general and first-instance jurisdiction handling all cases. The summary courts have original jurisdiction over civil cases involving claims not exceeding ¥900,000 and minor criminal offences.

The Supreme Court is only able to overturn its own interpretation of a law through the full Supreme Court. If a lower court's judgment does not follow the judgment rendered by the Supreme Court, the decision may be appealed. Therefore, although Japan does not, strictly speaking, adopt the common law system, as is the case in Hong Kong, the Supreme Court's judgments have a de facto binding effect on any court in subsequent cases.

Choice of Law (Act on General Rules for Application of Law)

The rules for choice of law, which will be taken by Japanese courts as international private law, is mainly governed by the Act on General Rules for Application of Laws.

The formation and effect of a juridical act, including without limitation contracts, shall be governed by the law of the place chosen by the parties. In the absence of such choice, the formation and effect of a juridical act shall be governed by the law of the place with which the act is most closely connected at the time of the act. In such case, if only one of the parties to a contract is to provide performance involved in a juridical act, the law of the habitual residence of

LAWS AND REGULATIONS

the party providing such performance shall be presumed to be the law of the place with which the act is most closely connected. In cases where the party has a place of business connected with the juridical act, this will be the law of the place of business. In cases where the party has two or more such places of business which are connected with the juridical act and which are governed by different laws, this will be the law of the principal place of business. The parties may change the governing law otherwise applicable to the formation and effect of a juridical act; provided, however, that if such change prejudices the rights of a third party, it may not be asserted against the third party.

Penal Code and the Code of Criminal Procedures

Crimes in Japan are mainly enumerated in the Penal Code, which provides the elements of different types of crimes and the penalties for different types of crimes. The Penal Code sets out minimum and maximum sentences for offences. Penalties range from fines and short-term incarceration to compulsory labour and the death penalty.

Under Article 31 of the Constitution, the requirements for constituting a crime under the Penal Code and any other criminal laws shall be construed strictly in accordance with the specific provisions contained in these laws. Any interpretations that rely upon analogy to other laws, or that look to similar treatment for actions under other laws, are prohibited. Therefore, under Japanese law, an act shall not be punishable unless such act is explicitly and clearly described as a crime under a strict contextual interpretation of the corresponding provisions.

A person shall not be subject to any criminal liability without procedural due process being observed under the Code of Criminal Procedures. Police have to secure warrants to search for or seize evidence. A warrant is also necessary for an arrest, although if the crime is very serious or if the perpetrator is likely to flee, it can be obtained immediately after arrest. Within forty-eight hours after placing a suspect under detention, the police have to present their case before a prosecutor, who is then required to apprise the accused of the charges and of the right to counsel. Prosecution will be denied if there is insufficient evidence or on the prosecutor's judgment. Most offences are tried first in district courts before one or three judges, depending on the severity of the case. Defendants are protected from self-incrimination, forced confession, and unrestricted admission of hearsay evidence. In addition, defendants have the right to counsel, public trial, and cross-examination.

Civil Code

(a) Structure of Civil Code

The Civil Code of Japan (民法 Minpo) was enacted in 1896. It was heavily influenced by the German Civil Code and the French Civil Code. The code is divided into five parts, the General Provisions, Property, Claims, the Family and Inheritance. The parts related to family and succession retain certain vestiges of the old patriarchal family system that was part of Japanese tradition. The Civil Code has remained substantially unchanged even after the American occupation in 1945, except for the fourth and fifth parts.

(b) Contract Law

As is the case for many countries, contracts under Japanese law are formed by the manifestation of intention by way of offer and acceptance. The parties may generally enjoy freedom to agree on the terms and conditions of any contract which will supersede most provisions of the Civil Code; however, some contracts may be subject to the mandatory requirements under the Consumer Contract Act and other applicable laws and regulations. The formation of contracts does not require documentation unless otherwise required under special

LAWS AND REGULATIONS

laws and regulations. Contrary to common law jurisdictions, consideration is not necessary for a contract to be enforceable. Also, there are no rules directly equivalent to the parol evidence rule in interpreting the terms and conditions of the contract.

(c) Torts

Under the Civil Code, a person who has intentionally or negligently infringed on any right of another, or a legally protected interest of another, shall be liable to compensate the other party for consequential damages. An employer is liable for damages inflicted on a third party by the actions of his/her employees in the execution of the employer's business; provided, however, that this shall not apply if the employer exercised reasonable care in appointing the employee or in supervising the employee's activities, or if the damages could not have been avoided even if he/she had exercised reasonable care. If more than one person has inflicted damages on another party or parties by their joint tortious acts, each of them shall be jointly and severally liable to compensate the other party or parties for those damages. The same shall apply if it cannot be ascertained which of the joint tortfeasors inflicted the damages.

(d) Property

Property rights are based upon the concept of ownership (title) under Japanese law. The owner of the property generally enjoys an absolute right to possess, utilise and dispose of the property, unless otherwise restricted under the mandatorily applicable laws or specifically agreed through a contract. Therefore, there is no concept of negative or affirmative covenants under Japanese law and the same purpose is achieved by mandatory laws in Japan (such as zoning or building or environmental laws and regulations) or by specific contractual arrangements.

Under the Civil Code, no type of property can be established other than those prescribed by laws including the Civil Code. The creation and transfer of property rights shall take effect solely by the manifestations of intention of the relevant parties. Any deed or written agreement is generally not required for the transfer of property (including land ownership) to be valid and enforceable under Japanese law and oral agreement is generally sufficient. However, the acquisition or loss of or any change in property rights concerning immovable property may not be asserted against a third party unless the same are registered pursuant to the applicable provisions of the Real Estate Registration Act (Act No. 123 of 2004) and other applicable laws and regulations regarding land registration.

REGULATORY FRAMEWORK

Our pachinko operations are subject to various requirements and restrictions under Japanese law and oversight by Japanese regulatory authorities. Generally, pachinko regulations fall under the Amusement Business Law and the cabinet and ministerial ordinances and regulations thereunder. In particular, the Amusement Business Law prohibits pachinko hall operators from being involved in the exchange of prizes for cash or securities by either providing cash or securities as prizes or repurchasing from customers the prizes provided to them. In order to ensure independence among pachinko hall operators, prize buyers and G-prize wholesalers, the pachinko industry operates under the "Three Party System" as described in greater detail below and in "Business — Pachinko Operations — Three Party System".

We are also subject to Japanese laws and regulations that require pachinko operators to obtain operating licenses and impose various operating requirements on pachinko halls and pachinko and pachislot machines, as well as other Japanese law and regulations applicable to Japanese companies generally, such as those relating to corporate governance, taxation and labour.

LAWS AND REGULATIONS

Pachinko is an established business and has been in place in Japan for more than five decades. The history of the pachinko industry has been characterised by government efforts to reform the industry to curb speculative excesses and perceived social problems relating to the industry. Prior to the later part of the period from 1995 to 1999, questionable business practices and crime and other anti-social forces gave the pachinko industry a negative public image. However, over the last two decades, the growing magnitude and importance of pachinko to the Japanese economy spurred the Japanese government and industry associations to step in to establish strict regulations, remove criminal and anti-social elements and improve the public image of the pachinko industry. The regulation effort has been highly successful. Due to the success of these reform efforts, the pachinko industry has evolved to become an integral part of the entertainment industry in Japan and an important component of the Japanese economy.

The following table sets forth the major regulatory developments that have affected the Three Party System over time.

<u>Date</u>	<u>Events</u>
17 July 1880 . .	The predecessor to the current Penal Code is first enacted, including provisions equivalent to the present provisions related to “Gambling” and “Running a Gambling Place for the Purpose of Gain” (Articles 260 and 261).
1904	The “Rule Regulating Gaming Places” is enacted.
24 April 1907 . .	The predecessor to the current Penal Code is amended, including provisions equivalent to the present provisions related to “Gambling”, “Habitual Gambling” and “Running a Gambling Place for the Purpose of Gain” (Articles 185 and 186).
1930	The first pachinko hall is opened in Nagoya.
1942 to 1945 . .	The pachinko hall business is banned during World War II as an unnecessary business in times of emergency.
10 July 1948 . .	The “Act Regulating Amusement Business” is enacted, under which pachinko hall operations became subject to licensing by the Public Safety Commission. Under this Act, each prefecture may set restrictions on amusement business operators, necessary to prevent harm to good morals (Article 3). Pursuant to this Article 3, prefectures begin promulgating local regulations prohibiting pachinko halls from: <ul style="list-style-type: none"> (i) providing cash as prizes; (ii) repurchasing from customers the prizes provided to them by those pachinko halls (the “Direct Repurchase Regulation”); and (iii) causing a third party to repurchase the prizes (the “Indirect Repurchase Regulation”).
10 November 1953	The Supreme Court holds that, if an operator of a gaming place, with a valid license from the Public Safety Commission under the “Act Regulating Amusement Business”, offers prizes within the scope of the license, it is an “activity involving betting for a thing that is provided for temporary amusement” under Article 185 of the Penal Code and thus is not gambling under the Penal Code.
1961	An early form of the Three Party System is adopted in Osaka.

LAWS AND REGULATIONS

<u>Date</u>	<u>Events</u>
17 June 1968. .	The Fukuoka High Court holds that there is no violation of the Direct Repurchase Regulation or Indirect Repurchase Regulation in local regulations, where prizes are commingled with prizes from other sources, because it is impossible to identify which of the prizes being purchased by the pachinko hall were originally from that same pachinko hall.
14 August 1984	The “Act Regulating Amusement Business” is renamed the “Act on Control and Improvement of Amusement Business, Etc.” (the “Amusement Business Law”), introducing the Direct Repurchase Regulation into the national legislation, and is substantially amended to prohibit, among others: (i) providing customers with cash or securities as prizes; and (ii) repurchasing from customers the prizes provided to them (Article 23).
August 1984 . .	Each prefectural government has in place local regulations ancillary to the Amusement Business Law as well as the Indirect Repurchase Regulation and Direct Repurchase Regulation.
11 January 1985	The “Ordinance for Enforcement of the Amusement Business Law” (the “Enforcement Ordinance”) is enacted, limiting the value of a prize offered by an amusement business to no more than ¥3,000.
25 September 1990	The Enforcement Ordinance is amended, raising the maximum limit on the value of a prize offered to ¥10,000 (Article 35, Paragraph 3).
17 April 1991 . .	The Penal Code is amended to raise the maximum amount of fine for a Crime of Gambling to ¥500,000 (Article 185).
25 June 2003. .	The National Police Agency answers questions raised by the “Group of Diet Members Considering Casino as an International Tourism Industry” and comments in support of the Three Party System in terms of both the Penal Code and the Amusement Business Law. The comments not only state that pachinko halls which operate their business within the scope of the Amusement Business Law are not engaging in “gambling” under the Penal Code, but also that third parties are not prohibited from purchasing prizes from pachinko hall customers.

LAWS AND REGULATIONS

Principal Administrative Authorities

The following are the principal administrative and regulatory authorities that oversee pachinko operations in Japan:

- the National Public Safety Commission;
- the Prefectural Public Safety Commission in the prefecture in which the relevant hall is located;
- police personnel;
- prefectural governments;
- the Security Communications Association;
- the Prefectural Entertainment Environment Cleanup Association; and
- the Minors Orientation Committee.

National Public Safety Commission

The National Public Safety Commission, an administrative commission belonging to the Japanese cabinet which oversees national security in Japan and implements regulations relating to the technical specifications of pachinko and pachislot machines as well as the operations of pachinko halls. For example, National Public Safety Commission regulations govern the playing costs of pachinko games, machine designs, maximum payout ratios and balls and pachislot tokens put into play and released, method of providing prizes, maximum value of prizes offered and the minimum age for playing pachinko.

The National Public Safety Commission also oversees the National Police Agency, which leads the prefectural police in their implementation of National Public Safety Commission regulations and policies.

Prefectural Public Safety Commission

The Prefectural Public Safety Commission in each prefecture is an administrative commission that supervises prefectural police agencies in their implementation of National Public Safety Commission policies and regulations. Each Prefectural Public Safety Commission grants pachinko hall licences, has the power to cancel pachinko hall licences, grants permission for changes in the structure of pachinko halls, certifies and approves pachinko and pachislot machines, approves the technical standards for pachinko and pachislot machines and monitors violations of laws and regulations by pachinko hall operators. It has authority, to the extent necessary for enforcement of the Amusement Business Law, to require holders of a pachinko hall licence to submit documentation concerning business matters. It also conducts hearings related to revocation, suspension or cancellation of pachinko hall licences or pachinko hall operations, and other related disciplinary actions against pachinko hall operators and pachinko hall managers.

Police personnel

Police personnel are permitted to enter pachinko halls to the extent necessary for enforcing the Amusement Business Law.

LAWS AND REGULATIONS

Prefectural governments

Prefectural governments set the standards for the hours of operation of pachinko halls, the level of noise and vibration around pachinko halls and collect fees which are necessary for certification, approval and examination of pachinko halls and pachinko and pachislot machines.

Security Communications Association

The Security Communications Association is responsible for examining machines to ensure that they comply with Amusement Business Law standards in their technical specifications and also to ensure that they do not promote a “passion for gambling”.

Prefectural Entertainment Environment Cleanup Association

The Prefectural Entertainment Environment Cleanup Association works under the Prefectural Public Safety Commission to organise personnel training and promote compliance with the Amusement Business Law.

Minors Orientation Committee

The Minors Orientation Committee works under the Prefectural Public Safety Commission to prevent minors from being involved in any “amusement business”.

Penal Code of Japan

Gambling is a criminal offence under the Penal Code of Japan (Act No. 45 of 1907, as amended). Article 185 prohibits “simple criminal gambling”, and violation is generally punishable by a maximum fine of ¥500,000. If the gambling is a repeated vice, it is considered “habitual criminal gambling”, which is prohibited by Article 186 and is punishable by up to three years’ imprisonment. Both types of gambling can be applied to a person engaged in the act considered to be gambling as well as to a person or entity who runs or organises a place for gambling. The Penal Code exempts activities that are expressly provided for in the laws and regulations of Japan, such as small-scale lotteries and public horse racing. Article 185 also exempts activities involving “betting for a thing that is provided for temporary amusement”. As a pachinko hall operator, the Company must therefore conduct its operations such that it only offers prizes that fall within the scope of “a thing that is provided for temporary amusement”.

The Supreme Court, the highest court in Japan, has upheld a lower court judgment holding that if a duly licenced operator of a gaming place offers prizes within the scope of its operating license granted by the Public Safety Commission under the Amusement Business Law, such act of offering such prizes is “an activity involving betting for a thing which is provided for temporary amusement” under Article 185 of the Penal Code and thus would not be deemed gambling under the Penal Code. In addition, the National Police Agency has stated that pachinko operators who are operating their businesses within the scope of the Amusement Business Law shall not be judged to have committed any act that constitutes the crime of gambling. As a result, the operations of pachinko operators who hold a valid operating license under the Amusement Business Law and offer prizes within the scope of their operating license are deemed to fall within the exemption to the prohibition on gambling under the Penal Code. Our Japan Legal Adviser, after conducting the due diligence searches described under “ — The Three Party System” below, have confirmed that we hold a valid operating license under the Amusement Business Law and our prizes are offered within the scope of our operating license, and our pachinko operations thus do not violate the Penal Code.

LAWS AND REGULATIONS

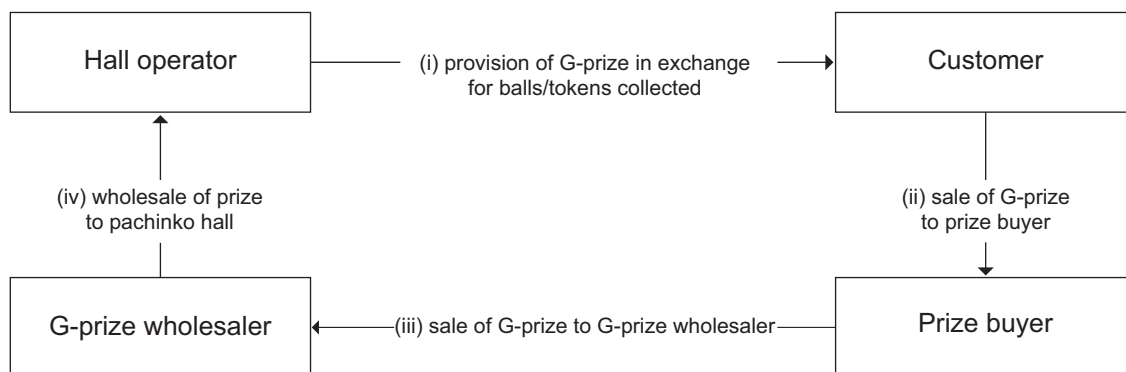
Amusement Business Law

The Amusement Business Law sets regulations for “amusement businesses” such as pachinko. It sets out requirements and regulations that pachinko hall operators must comply with in order to operate their halls. Article 23 of the Amusement Business Law prohibits pachinko hall operators from being involved in the exchange of prizes for cash or securities by either providing cash or securities as prizes or repurchasing from customers the prizes provided to them for cash or securities. It does not prohibit a customer from selling a G-prize redeemed in a pachinko hall to a third party who is not the pachinko hall operator. Nor does it prohibit the pachinko hall from purchasing a G-prize from a third party. However, there are local regulations established by prefectural governments which prohibit pachinko hall operators from causing third parties to repurchase G-prizes from customers (the “Third Party Regulations”). The application of the Amusement Business Law to the Three Party System is described further in the section below.

The Three Party System

Under the “Three Party System”, a pachinko hall operator, a prize buyer and a prize wholesaler participate in the sale and purchase of G-prizes obtained by a customer of the pachinko hall operator by playing pachinko and pachislot games. G-prizes are supplied to pachinko operators by wholesalers. Wholesalers may serve various pachinko operators with the same type (in design and appearance), of G-prizes. As a result, G-prizes may not be distinguished by the pachinko operator.

The Three Party System can be illustrated as follows:



As illustrated above, a customer, who has changed cash into pachinko balls or pachislot tokens and then plays pachinko or pachislot games, may exchange the balls or tokens at the hall for a G-prize. These pachinko balls or pachislot tokens are exchanged for G-prizes at a mark-up, set by the pachinko hall, over the purchase price of the G-prize paid by the hall operator to the G-prize wholesaler. A customer may, but is not obliged to, present such G-prizes to a prize buyer, who will purchase the G-prize from the customer for a cash amount equal to the amount at which the wholesalers will purchase such G-prize from the prize buyer, which in turn is equal to the purchase price paid by the hall operator to the G-prize wholesaler for such G-prize. See “Business — Three Party System — Agreements with G-prize wholesalers”. Wholesalers purchase G-prizes from various prize buyers and sells the G-prizes to various pachinko halls. Because all the G-prizes purchased by the wholesaler from multiple prize buyers are commingled, the G-prizes that are sold to the pachinko hall by the wholesaler are not necessarily the same G-prizes provided by the pachinko hall to its customers.

LAWS AND REGULATIONS

The National Police Agency has commented that the Amusement Business Law only regulates pachinko hall operators, but not persons or entities unrelated to the pachinko hall operator, hence an unrelated third party is not prohibited from purchasing G-prizes from customers. Accordingly, the prevailing interpretation of the National Police Agency in its administration of the Amusement Business Law and the Third Party Regulations is that an unrelated third party's purchase of G-prizes from a pachinko player is, subject to compliance with the industry practices as described in this section that have evolved under the prevailing interpretation of the Amusement Business Law in the purchase and sale of G-prizes, legal under the Amusement Business Law. In this regard, Japanese courts and the National Police Agency have determined that pachinko industry practices in the purchase and sale of G-prizes, involving multiple types and originating from multiple sources, including pachinko halls and hall operators, wholesalers and prize buyers, comply with the requirements of the Amusement Business Law. In determining whether a prize buyer is an unrelated third party, and whether a pachinko hall's purchase from such prize buyer is legal in accordance with the prevailing interpretation of the National Police Agency, the following factors must be satisfied: (1) neither party may have the ability to exercise control, whether directly or indirectly, over the other, through (i) any relationship or connection between the personnel of the prize buyer and pachinko hall; (ii) any equity holding or any other capital relationship or connection between the prize buyer and pachinko hall; or (iii) any contract or other agreement between the prize buyer and pachinko halls; (2) G-prizes to be purchased are of market value; and (3) G-prizes are not directly returned from the prize buyer to the pachinko hall.

Each of these factors are satisfied with respect to our pachinko halls. With respect to the first factor, neither our pachinko halls nor the prize buyers have any ability to exercise control over the other, there is no relationship or connection between the personnel of our pachinko halls with those of the prize buyers, and there is no business relationship or equity holding or any other capital relationship or connection between our pachinko halls and the prize buyers. The second and third factors are also satisfied as the G-prizes purchased by the prize buyers have intrinsic value (such as that attributed to the piece of gold or silver embedded in the prize), and there is no direct sale of G-prizes by the prize buyer to the pachinko hall from which the customer obtained the G-prize. Rather, G-prizes are commingled by wholesalers with a variety of G-prizes, ensuring that G-prizes purchased by the pachinko hall are not necessarily the same G-prizes as those purchased by the prize buyer. In order to maintain the independence of our pachinko halls from the prize buyers, we ensure that none of our management, Directors and staff are engaged in the prize buying business.

In addition, because the pachinko hall and the wholesaler must also maintain independence with respect to each other, neither party may have the ability to exercise control, whether directly or indirectly, over the other, through (i) any relationship or connection between the personnel of the pachinko hall and the wholesaler, (ii) any equity holding or any other capital relationship or connection between the pachinko hall and the wholesaler, or (iii) any contract or other agreement between the pachinko hall and the wholesaler.

Each of these factors are also satisfied with respect to our pachinko halls. There is no relationship or connection between the personnel of our pachinko halls with those of the wholesalers and there is no equity holding or any other capital relationship or connection between our pachinko halls and the wholesalers. We adopt the following internal control procedures to ensure the independence of our pachinko halls from our G-prize wholesalers:

- we engage independent third parties to perform annual searches on the shareholding structure and list of directors for all of our G-prize wholesalers to ensure there is no overlapping of shareholders and directors between our Group and our wholesalers;

LAWS AND REGULATIONS

- we require existing G-prize wholesalers to report any change in shareholding structure and composition of their board of directors in a timely manner;
- we obtain written declarations annually from all of our G-prize wholesalers stating their independence from our Group; and
- we require potential new G-prize wholesalers to provide lists of their shareholders and directors and submit independence declarations, and cross check with the search results performed by independent third parties before the engagement to ensure there is no overlapping of shareholders and directors between our Group and any new G-prize wholesalers.

Our Japan Legal Adviser has advised us that as long as the Three Party System is structured in accordance with prevailing standard industry practices in the pachinko industry, which is followed by us in our operations, and the factors described above are otherwise satisfied, our pachinko operations do not violate the Third Party Regulations or the Amusement Business Law. In this regard, our Japan Legal Adviser, after conducting due diligence searches, has also determined that each of our pachinko halls is independent as evaluated under the factors listed above, from its prize buyers and from its G-prize wholesalers. The due diligence investigation undertaken by our Japan Legal Adviser included the following:

- interviews with the Directors, and if applicable other responsible personnel, of the Company and its subsidiaries;
- review of all the sale and purchase agreements of G-prizes entered into between the Company or any of its subsidiaries and each of the G-prize wholesalers;
- review of written declarations from the G-prize wholesalers confirming that each of them is independent from the prize buyers with whom they contract;
- review of all commercial registry certificates of the G-prize wholesalers; and
- review of all the Operating Licences of all the pachinko halls operated by our Group.

The due diligence investigation undertaken by the Joint Sponsors regarding the independence of the G-prize wholesalers and prize buyers included the following:

- independent shareholder and director searches on the G-prize wholesalers;
- interviews with the G-prize wholesalers regarding, among others, the nature and extent of their relationships with the Group and their relationships with the prize buyers with whom they conduct business;
- confirmations from the G-prize wholesalers confirming that each of them has no ability to control the Company and its subsidiaries;
- confirmations from the Directors that none of them is, and at all times was not, a connected person of any G-prize wholesaler;
- confirmations from the Directors that neither the Company nor each of them, as individuals, is not, and at all times was not, engaged in any prize buying business or a connected person of any prize buyer;
- review of the master agreements with the G-prize wholesalers; and

LAWS AND REGULATIONS

- confirmations from the G-prize wholesalers to the Company that there is no capital connection or shared staff with the prize buyers with whom they conduct business.

The National Police Agency has never taken any action against the legality of the pachinko business or the Three Party System. We have been advised by our Japan Legal Adviser that, based on certain court cases, governmental statements and practices, the Three Party System does not violate the Amusement Business Law, nor does it constitute gambling under the Penal Code of Japan. As at the Latest Practicable Date, we have not been found to be in breach of any provision of the Amusement Business Law or the Penal Code of Japan and our Japan Legal Adviser, after conducting due diligence searches, is of the opinion that our pachinko operations do not contravene the Amusement Business Law or the Third Party Regulations. Based on the foregoing, in the opinion of our Japan Legal Adviser, our pachinko operations carried out in the context of the Three Party System do not contravene either the Third Party Regulations or the Amusement Business Law.

REGULATIONS ON PACHINKO OPERATIONS

Pachinko hall business licence

The pachinko hall business is considered an “amusement business” as prescribed by the Amusement Business Law and other relevant laws, regulations, and prefectural ordinances. Under the Amusement Business Law, a pachinko hall operator must obtain a licence (an “Operating Licence”) from the Prefectural Public Safety Commission prior to establishing each pachinko hall. Once granted, the Operating Licence will continue to be effective unless and until it is cancelled by the Prefectural Public Safety Commission pursuant to the Amusement Business Law.

When considering an application for an Operating Licence, the Prefectural Public Safety Commission will consider the following factors prescribed by the Amusement Business Law:

- whether the business owner/operator is, with reference to past offences or other instances of regulatory non-compliance, a fit and proper person to hold an Operating Licence (the “Fit and Proper Person Requirements”);
- the proposed place of business, including its structural integrity and other building specifications;
- the location of the intended place of business, including town planning and area zoning considerations and proximity to schools and hospitals; and
- the compliance with legal specifications of the pachinko and pachislot machines intended to be installed at the proposed hall.

The Prefectural Public Safety Commission may, at its discretion and at any time, impose conditions on the Operating License which it considers necessary in order to maintain certain standards of moral decency within the pachinko hall and broader food and beverage industry and otherwise for the protection of minors.

Other significant limitations on the holder of an Operating Licence (the “Licence Holder”) include restrictions on corporate restructuring and corporate succession, so as to prevent the unauthorised transfer of an Operating Licence. The Prefectural Public Safety Commission must grant prior approval to any corporate restructuring carried out by a holder of an Operating Licence in the relevant prefecture. Any Operating Licence transferee is subject to the same requirements as the original Licence Holder.

LAWS AND REGULATIONS

The Prefectural Public Safety Commission has broad authority to issue directives or impose sanctions on a Licence Holder, including its business representatives and employees, in circumstances where there has been a breach of the Amusement Business Law or other civil and criminal laws.

The Prefectural Public Safety Commission may cancel an Operating Licence, or issue a directive to suspend operations carried on thereunder, where:

- it has been obtained through fraudulent or other illegal means;
- the Licence Holder no longer satisfies the Fit and Proper Person Requirements;
- the pachinko business has not commenced within six months from the grant of an Operating Licence or there has been any suspension of operations for more than six months without justifiable grounds;
- the whereabouts of the Licence Holder is unknown for more than three months;
- the Licence Holder breaches any legislation pertaining to the business which is the subject of the Operating Licence, and such violation is likely to:
 - cause substantial harm to a good and quiet moral environment; or
 - violate the rights of minors; or
- the Licence Holder fails to comply with a directive of the Prefectural Public Safety Commission or a license condition.

In the event that the pachinko operator has an objection to the cancellation or suspension of an Operating Licence, it may, within six months from such decision, bring an action with the relevant court for the revocation of the administrative decision.

As at the Latest Practicable Date, we had obtained 355 licences for our pachinko hall operations, each of which is currently valid. Our Group's Operating Licences, and the validity of each Licence, were not affected by the Great East Japan Earthquake.

Pachinko and pachislot machine regulations

The Amusement Business Law, and the enforcement regulations prescribed under the Amusement Business Law, also regulate pachinko and pachislot machines installed in pachinko halls by the Licence Holder. One of the Operating Licence conditions is that pachinko and pachislot machines installed in pachinko halls do not encourage a "passion for gambling".

Pachinko and pachislot machines are subject to certain restrictions, such as those listed below, in order to comply with this condition:

- limitations on the value of pachinko balls or pachislot tokens that may be put into play per minute;
- limitations on the number of pachinko balls or pachislot tokens that may be released in various modes of play;
- limitations on the total number of pachinko balls or pachislot tokens that may be released over a continuous period of play;

LAWS AND REGULATIONS

- the size of the pockets which trigger jackpot mode, as compared to the size of the pachinko ball, may not be significantly larger or smaller than the customary size;
- pachinko balls may not be automatically fired into the field of play without the player directly controlling the shooting strength; and
- the machine may not be capable of easily being illegally modified or otherwise changed.

A person who intends to manufacture or import a pachinko or pachislot machine or to install it may, but is not legally required to, apply for an inspection of the machine by the Security Communications Association for specifications of such imported or manufactured pachinko or pachislot machine. A machine manufacturer typically submits its machine prototypes to testing by the Security Communications Association. Machine prototypes that pass such testing receive certificates. Each machine subsequently manufactured according to that prototype will also have a certificate showing its compliance with such testing. Purchasing machines from manufacturers that have received this approval reduces the risk of installing machines that do not comply with the legal requirements. A pachinko operator that intends to increase or change its number of machines, including the transfer of a machine to a different pachinko hall, must obtain prior written permission from the Prefectural Public Safety Commission.

Because we only purchase machines from manufacturers that submit their machine prototypes for testing by the Security Communications Association, our pachinko and pachislot machines each have a certificate demonstrating compliance with those tests and have passed all inspections conducted by the relevant Prefectural Public Safety Commission during the Track Record Period.

Adjustment of pins

Under the Amusement Business Law, the pachinko hall must obtain permission from the Prefectural Public Safety Commission before making any changes to an installed pachinko or pachislot machine. Therefore, a machine which has been tested and approved by the Security Communications Association and the relevant Prefectural Public Safety Commission, should not be altered after it is installed. This requirement prevents improper modifications that may change the machine beyond the permissible range of operation.

Pins often shift during the normal course of play on a pachinko machine as the pachinko balls cascade down, through and collide into the pins in the playing field. Consistent with industry practice, we generally perform daily adjustments on the angle of the pins and pinwheels in order to maintain compliance with, among others, the limitations on payouts and jackpot mode. These adjustments do not require prior approval from the National Public Safety Commission.

No court cases have considered the definition or interpretation of “change” to a pachinko machine, so far as it relates to the adjustment of pins as described above; however, under current practices, it is generally understood that the adjustment of pins would not be construed as a “change” in pachinko machines if the following three criteria are satisfied:

- the pin adjustment does not involve any bending or other modification of the shape of the pins;

LAWS AND REGULATIONS

- the purpose of the pin adjustment is to comply with the specification restrictions with respect to each pachinko machine, and to maintain the permissible average ball release rate of the hall's overall pachinko operations; and
- the pachinko machine for which the pin adjustment has been performed continues to be in compliance with the specification restrictions listed above.

Our Japan Legal Adviser, after conducting due diligence investigations (which included interviews with the responsible officers of the Company and a review of written explanations prepared by the legal department of the Group), has confirmed that we have strictly complied with the three criteria listed above regarding the adjustment of pins and are in full compliance with the requirements of the Amusement Business Law.

Trading used pachinko machines

The license, approval or permit requirements under Japanese law and regulations for dealing in pachinko and pachislot machines are limited to a permit for dealing in second-hand goods under the Used Goods Dealer Act. This permit is issued by the Prefectural Public Safety Commission.

It is also customary for dealers of pachinko machines to register as such with the Japan Amusement-Related Business Association, and to obtain a registration certificate. Without this registration certificate, pachinko operators will refuse to deal with such unregistered dealer. Kanto Daido has obtained both a registration certificate and a permit under the Used Goods Dealer Act.

Playing costs, prize offerings and prize value

The Amusement Business Law and the National Public Safety Commission regulations regulate pachinko and pachislot playing costs, the offering of prizes and the upper limit of the value of prizes.

The Regulations prescribe the following playing costs:

Pachinko machine	Machine that uses balls	4 yen or less per ball
Pachislot machine	Machine that uses tokens	20 yen or less per token

The value of prizes offered may not exceed ¥10,000, and the types of prizes are generally limited to everyday general consumer goods, such as snacks, beverages, cigarettes and sundry household items. Our Japan Legal Adviser has confirmed that G-prizes, which include decorative cards with a small embedded piece of gold or silver and coin shaped pendants of gold or silver, comply with this regulation. The market value of the prizes offered must also be equivalent to the value of the pachinko balls or pachislot tokens redeemed by the player for such prizes. In addition, in order for the prizes to meet the diverse range of expectations of customers, the hall must offer as prizes a wide range of items suitable for everyday use.

The Amusement Business Law prohibits Licence Holders from:

- offering cash or securities as prizes;
- buying back prizes awarded to customers; and
- allowing customers to take pachinko balls, pachislot tokens or any other similar objects provided for playing pachinko or pachislot outside the hall.

LAWS AND REGULATIONS

Offering cash or securities as prizes constitutes a breach of the Amusement Business Law, and as a result the pachinko operator may be subject to suspension of business for a period ranging from 20 days to 180 days as an administrative sanction. In addition, a penalty of imprisonment up to six months, or a fine of ¥1 million may be imposed as criminal sanctions.

Membership systems

The Amusement Business Law prohibits Licence Holders from issuing any written documentation indicating that pachinko balls or pachislot tokens are being held for a customer. However, Article 16-9(2) of the Standards for the Interpretation and Operation of the Act on Control and Improvement of Amusement Business issued by the National Police Agency provides that a membership card does not constitute written documentation of the hall holding balls or tokens for a customer if the number of such balls or tokens is not recorded on the card itself and is stored only on computers in the halls.

Our Japan Legal Adviser has verbally consulted with the National Police Agency regarding the relevant provisions of the Amusement Business Law and Article 16-9(2) of the Standards for the Interpretation and Operation of the Act on Control and Improvement of Amusement Business and has confirmed that our membership system does not constitute written documentation of balls or tokens being held for customers.

Operating hours and restrictions

The Amusement Business Law restricts pachinko hall opening hours to the period from sunrise to 12:00 a.m. However, each prefecture is permitted to impose more stringent limits on operating hours and such additional restrictions are common. In Tokyo, for example, halls are prohibited from operating between 11:00 p.m. and 10:00 a.m. the following day.

In addition, customers are forbidden from taking pachinko balls or pachislot tokens from the pachinko halls and therefore are deemed to “rent” the balls or tokens with which they play pachinko or pachislot.

Environmental regulations

A Licence Holder must conduct business in such a way as not to cause noise or vibrations (limited to voices of people and other noises and vibrations that are part of operating a business) in the area surrounding the place of business that exceed the limits specified by prefectural ordinances.

LAWS AND REGULATIONS

The Amusement Business Law prescribes the following noise limits:

<u>Regional</u>	<u>Numerical Value</u>		
	<u>Daytime</u>	<u>Evening</u>	<u>Late Night⁽¹⁾</u>
(1) In areas specified by a particular prefecture in a prefectural ordinance as necessary to be especially quiet due to condensed housing or other similar areas.	55 decibels	50 decibels	45 decibels
(2) In areas specified by a particular prefecture in a prefectural ordinance as necessary not to have extreme noise due to condensed stores and other similar areas.	65 decibels	60 decibels	55 decibels
Areas other than the areas in (1) and (2) above . .	60 decibels	55 decibels	50 decibels

(1) "Late Night" refers to 12:00 a.m. until sunrise.

Advertising and promotion regulations

The Amusement Business Law requires a Licence Holder to advertise or promote their business in such a way that it will not likely interfere with the peace and quiet surrounding the place of business. Under the published guidelines, the following methods of advertisement are likely to constitute an "interference with peaceful and quiet surroundings":

- displaying sexually explicit or other adult material;
- advertising or promoting the manipulation of pins or otherwise encouraging customers' "passion for gambling"; or
- noise levels beyond prescribed limits in public areas.

Prohibition on minors

Customers of pachinko halls must be at least 18 years of age. The Amusement Business Law provides that the Licence Holder must post a sign at the entrance to the place of business prohibiting entry by those under the age of 18. The sign must be posted so as to be easily seen by the public.

Building and construction regulations

If a Licence Holder adds to the structure, makes structural changes or undertakes any other construction or changes to the facilities of the place of business, it must obtain prior permission from the Prefectural Public Safety Commission, with the exception of some specified minor changes.

Examples of structural or equipment modifications that require permission include extensive repairs to the place of business, changes to the location of guest rooms or floor space, and changes to the facilities such as adding walls or Japanese-style sliding doors to partition the interior of the place of business.

LAWS AND REGULATIONS

We must comply with the Building Standard Act, which requires any entity that constructs, substantially repairs or remodels, whether by itself or through a third-party contractor, any building that is larger than a certain scale or that is located in certain designated areas to obtain a certificate of prior confirmation for the planned construction, repair or remodelling as well as a certificate of completion thereof from an inspector appointed by the local authorities.

We must also comply with the City Planning Act, which designates areas where certain usage is not allowed. No Operating Licence will be granted unless the pachinko hall is located in an area where it is permitted under the City Planning Act.

ANTI-MONEY LAUNDERING

The anti-money laundering laws in Japan do not impose any specific obligations on pachinko operators. Unlike casino gaming, where customers purchase casino chips that have little or no intrinsic value but have high face values and have the potential to win or lose substantial sums in a short period of time, pachinko presents the opportunity over a relatively long period of time to win G-prizes that have a limited intrinsic value. The inherent mechanical limitations on pachinko ball and pachislot token dispensers render it extremely difficult for a pachinko player to obtain the number of pachinko balls or pachislot tokens necessary to redeem G-prizes of significant value in a short period of time as a ball or token dispenser can only release about 750 balls or 600 tokens per minute. Thus, a customer seeking to launder even an insignificant amount of cash would need to spend at least several hours exchanging the cash into balls or tokens in addition to a considerably longer period of time putting such balls or tokens into play in a machine.

Furthermore, we do not allow customers to exchange balls or tokens into prizes without first putting them into play in the machines and we have put in place internal policies and internal control measures to prevent customers from violating this requirement. Our hall staff closely monitor the number of balls rented and the number of balls played in each of the machines. Any irregularities in such numbers are closely followed up by hall staff. Surveillance cameras are also installed in the pachinko hall, and hall staff patrol the pachinko hall during its operating hours in order to detect any suspicious activity. Thus, it would be inefficient and highly impractical to engage in money laundering activities through pachinko or pachislot. For more information on our anti-money laundering procedures, see “Internal Controls and Anti-Money Laundering — Internal Controls on Money Laundering”.

LABOUR PROTECTION

The Industrial Safety and Health Act (Act No. 57 of 1972) provides standards for employers regarding the health and safety of employees including the employer’s responsibilities and plans for accident prevention in the workplace. An employer with more than 50 employees must take reasonable measures to prevent workplace accidents, and must also make efforts to protect employees from the risk of passive smoking.

Anti-Smoking

Under the Health Promotion Act (No. 103 of 2002), a person who has control over a facility used by many people must endeavour to prevent passive smoking in the facility. A pachinko hall is deemed to constitute such a facility, as it is used by many people. Also, under the Industrial Safety and Health Act (Act No. 57 of 1972), an employer must endeavour to make the workplace comfortable for employees, and based upon this provision, the Ministry of Health, Labour and Welfare has implemented guidelines to promote the prevention of passive smoking in the workplace. These guidelines do not impose any legal obligation on, nor any penalties or sanctions for noncompliance by, facility operators. Amendments to the Industrial Safety and

LAWS AND REGULATIONS

Health Act have been proposed but the discussion has been postponed to the next Diet session, which may result in more stringent guidelines or create obligations with respect to the prevention of passive smoking. Also, there are a variety of laws and regulations adopted and enforced, and others which have been proposed, at the local and prefectural levels restricting smoking. Generally, these local anti-smoking laws establish exemptions from their application to establishments such as bars, restaurants and pachinko halls.

PERSONAL INFORMATION PROTECTION

The Personal Data Act requires that a Japanese business operator handling personal information must limit the use of personal information to the stated purpose and to properly manage the personal information in their possession, and forbids it from providing personal information to third parties without the consent of the individual.

INTELLECTUAL PROPERTY REGULATIONS

In Japan, patents are protected by the Patent Act and the Utility Model Act (Act No.123 of 1959). Designs are protected by the Design Act (Act No.125 of 1959), and trademarks by the Trademark Act (Act No.127 of 1959). We must comply with these, in addition to various international treaties Japan has entered into, to maintain our intellectual property rights.

TAXATION

Dividends tax

Generally, non-resident Shareholders are subject to Japanese withholding tax on dividends paid by Japanese corporations. Such taxes are withheld prior to payment of dividends as required by Japanese law. Stock splits are, in general, not a taxable event. In the absence of an applicable tax treaty, convention or agreement reducing the maximum rate of Japanese withholding tax or allowing exemption from Japanese withholding tax, the rate of Japanese withholding tax applicable to dividends paid by Japanese corporations to non-resident Shareholders is generally 20%.

Our Tax Adviser has confirmed that Japanese tax laws recognise the CCASS Beneficial Owners, being the ultimate payees of the dividend, as taxpayers. As such, the withholding tax rate applicable to the dividend paid to CCASS Beneficial Owners is, in principle, the tax rate applicable to each beneficial owner on an individual basis in accordance with their identity, shareholding percentage, and tax residence. However, because we are unable to ascertain the identity, and consequently the tax residence, of the CCASS Beneficial Owners due to the inherent characteristics of CCASS, we are unable to apply a rate of withholding tax on an individual basis to such CCASS Beneficial Owners. As a consequence, we will, upon distribution, apply a withholding tax on the entire amount of the dividend payable to the CCASS Beneficial Owners at the highest possible withholding tax rate under Japanese law.

Under the Hong Kong-Japan Tax Treaty, the Japanese withholding tax rate that applies to dividends payable to a beneficial holder of Shares who is a Hong Kong resident is reduced to a rate not exceeding 10% (or not exceeding 5% for corporate Shareholders who are interested in 10% or more of the voting Shares of our Company for the six months ending on the record date for dividend distribution). As a general rule, a beneficial owner of Shares (other than CCASS Beneficial Owners) who is entitled to a reduced rate of Japanese withholding tax on payments of dividends is required to submit an Application Form for Income Tax Convention Regarding Relief from Japanese Income Tax on Dividends (together with other required forms and documents) in advance, through the withholding agent to the relevant tax authority before the payment of dividends. However, a beneficial owner who does not submit an application in advance will be

LAWS AND REGULATIONS

entitled to claim a refund from the relevant Japanese tax authority of the taxes withheld in excess of the applicable tax treaty rate by complying with certain subsequent filing procedures. CCASS Beneficial Owners will only be able to claim a refund of withholding taxes after dividends are distributed to them. A standing proxy for the beneficial owner may make the application on his behalf. The Hong Kong-Japan Tax Treaty would apply to a non-resident of Japan Shareholder who is a resident of Hong Kong.

For further information, see “Material Shareholders’ Matters under Japanese Law — Dividends — Japanese withholding tax for dividend payments”.

Capital gains tax

Under the Hong Kong-Japan Tax Treaty, non-resident Shareholders are generally not subject to taxation for capital gains on a transfer our Shares. For further information on capital gains tax in Japan, see “Appendix III — Summary of Articles of Incorporation, the Companies Act and Taxation in Japan”.

Estate and gift tax

Japanese inheritance tax and gift tax at progressive rates may be payable by an individual who has acquired ordinary shares of our Company as a legatee, heir or donee even though neither the acquiring individual nor the deceased nor donor is a Japanese resident.

OTHER

A Japanese company must, upon incorporation, register with the legal affairs bureau and continue to update its details from time to time. It must also register with the local tax agency and must annually report on corporate tax, value added tax or other taxes.