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# Development/Operation and Securitization Structures of a Data Center in Japan

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## 1. Data Center

A data center is a dedicated facility specially built for installing servers and network equipment, and is used for a wide range of purposes, including cloud service operations, data storage, and development of artificial intelligence (AI). Inside the facility, there are racks for placing servers and space for installing network equipment. Data centers are also equipped with various systems that are necessary to operate servers such as high-speed Internet and other external connection lines, cooling apparatus, and a high-capacity power supply.

There are two major data center services: (i) “housing” or “co-location,” which involves leasing a facility for servers and other equipment; and (ii) “hosting,” which is leasing servers and other equipment used in the data center. “Housing” and “co-location” are services for leasing the physical building of the data center or racks to place servers and spaces to install equipment. Although these terms are not specifically defined, “housing” is generally used for leasing dedicated racks, and “co-location” is used for leasing dedicated spaces.

“Hosting” is a service to lease servers and network equipment provided by the data center, which is why this service is also called “rental servers.”

## **2. Development and Operation of a Data Center**

### **(1) Development of a Data Center**

Development of a data center involves the acquisition of a site and construction of a building.

Depending on the location and scale of the data center, it will be necessary to review the National Land Use Planning Act, the City Planning Act, the Building Standards Act, and other laws and ordinances regulating development. In addition, if it is necessary to purchase or lease land from landowners, the Civil Code, the Building Lots and Buildings Transaction Business Act, the Act on Land and Building Leases, the Immovable Property Registration Act, and other relevant laws and ordinances must also be reviewed.

Although it depends on the location and the current condition of the site to be acquired, an acquisition of a large site owned by a number of landowners would require coordination of the landowners, and development of a site that is in an Urbanization Control Area or is classified as Farmland would require certain permits and approval from the relevant authorities. It is also necessary to consider alternative measures for a potential refusal by some landowners to sell their land, conditions regarding responses to administrative authorities to be stipulated in the land purchase or lease contract, and other actions, bearing in mind the risk of failure of the project.

Moreover, attention must be paid to the Forest Act, the River Act, the Environmental Impact Assessment Act, the Noise Regulation Act, the Landscape Act, the Act on Promotion of Global Warming Countermeasures, and other regulations and ordinances. When carrying out development, it is also necessary to pay attention to the Building Standards Act, the Fire Service Act (including fire prevention and other related ordinances), the Landscape Act, etc., as well as to examine ordinances concerning harmony and integration with residents and the living environment in that area.

As data centers consume a large amount of power and require access to high-voltage electricity through multiple power receiving grids, power supply contracts need to be entered into and it may take considerable time and cost to install new power lines.

### **(2) Operation of a Data Center**

Both users and the operator (owner) of a data center need to enter into complex contracts, including leases for server rooms and server racks, contracts for the use of software and electricity, contracts for access control systems for electronic locks, and contracts for the use of offices, data storerooms, warehouses, and cabinets, among others.

In most cases, when a data center operator's service is providing space for installing a server, it is typically considered a lease to the user. In this respect, applicable laws and ordinances may vary depending on the contents and specific circumstances of the services provided by the data center operator, including applicability of the Act on Land and Building Leases. Therefore, this aspect should also be considered when providing these types of services.

## **3. Securitization Structures Pertaining to the Development of and Investment in Data Centers**

From the aspect of development and investment in a data center, the following investment (securitization) structure are possible, using a special purpose company, or similar investment vehicle.

### **(1) GK-TK Structure**

For the purpose of investing in the development of a data center, it is possible to use a GK-TK structure in which investors are silent partners and a special purpose company (SPC) is the proprietor. This is an

investment structure based on a silent partnership agreement as provided for in Part II, Chapter IV of the Commercial Code, under which investors are silent partners and an SPC such as a *gōdō kaisha* (GK) is the proprietor.

It should be noted that when a silent partner invests in real estate directly, this investment will be subject to the Act on Specified Joint Real Estate Ventures. However, a structure using an SPC can avoid this application of the Act on Specified Joint Real Estate Ventures by setting the investment target as trust beneficiary rights regarding the real estate. On the other hand, it is also possible for an SPC to invest in real estate directly by entrusting the real estate transaction to a specified joint real estate enterprise and submitting notification for conducting a Special Venture.

## **(2) TMK Structure**

It is also possible to make investments using a *tokutei mokuteki kaisha* (TMK) under the Act on the Securitization of Assets. Unlike the GK-TK structure, this structure legally ensures the “conduit requirements,” and therefore dual taxation to the vehicle (TMK) and investors can be avoided. Also, the asset manager is not subject to the Financial Instruments and Exchange Act.

However, a TMK is required to carry out its business based on an asset securitization plan which is submitted to a Local Finance Bureau. In addition, the trustee entrusted with the administration and disposition of the real estate (the specified assets) needs to be a real estate broker unless a trust is created. There are also a variety of other regulations including a prohibition of engaging in other businesses and an obligation to fulfill requirements under the Act on Special Measures Concerning Taxation regarding the inclusion of dividends in deductible expenses.

## **(3) LPS (Investment Limited Partnership) Structure**

An investment limited partnership agreement (LPS agreement) can be used to invest in the development of a data center. Partners under an LPS agreement must consist of both unlimited liability partners and limited liability partners. A possible structure using this partnership is for an SPC to act as an unlimited liability partner, investors to act as limited liability partners, and the SPC to perform special business activities for qualified investors, or alternatively to entrust this business to an investment manager.

Also, since direct investment in real estate is not allowed under an LPS agreement, investment targets need to be beneficial interests of trusts or silent partnership equity securities. This structure is subject to certain requirements such as implementation of statutory audits; however, each partner is responsible for their own tax payments.

## **4. Related Articles**

[“Legislation/Contracts and Securitization Structure Concerning Development etc. of a Data Center”](#) (in Japanese)

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