

Opinion Paper for Drafting the Corporate Governance Code (For the 4th Council)

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1. Disclosure and Transparency

(1) Disclosure-related matters

In addition to ensuring timely and accurate disclosure, we should aim at enhancing the quality of the information to be disclosed.

For example, recently, amid a growing focus on constructive dialogue between companies and investors, or so-called engagement, to create sustainable corporate value, there has been a growing expectation for non-financial information disclosure such as companies' objectives, basic policies and implementation procedures of corporate governance, and managerial strategies. Therefore, in accordance with the globally spreading integrated report proposed by International Integrated Reporting Council (IIRC) , **we should facilitate the disclosure of non-financial information, for instance, by incorporating the disclosure of such an integrated report in the Corporate Governance Code.**

Under the 'comply or explain' approach, companies may adopt practices other than those shown in the Code; provided that such adoption further enhances long-term corporate value and that the companies provide explanations. With regard to this explanation, **the Code should stipulate that companies must provide concrete and rational explanations, avoiding 'boilerplate' disclosure.**

(2) Disclosure of Remunerations for the Members of the Board of Directors and Key Executives

From the viewpoint of 'offensive governance' to enhance earning power, it is essential that the calculation method, rather than the individual remuneration amounts, serves as an appropriate incentive for the Board members and key executives to increase growth and profitability of their company.

Accordingly, **companies should establish a remuneration committee (or a remuneration advisory committee in case they are not 'Companies with Committees'), the majority of which consists of independent directors, and then disclose their policies and procedures for determining remunerations for directors which provide appropriate incentives.**

Furthermore, in order to provide incentives to increase growth and profitability of companies, the policies for determining remunerations of the Board members and key executives should put more weight on remuneration portions linked with medium to long-term business performance.

(3) Disclosure of Qualifications and Selection Processes of the Board Members and Key Executives

As mentioned below, the selection/dismissal of the Board members, including Chief Executive Officer (CEO), and key executives is the most important matter for 'offensive governance'.

Accordingly, **companies should establish a nomination committee (or a nomination advisory committee in case they are not 'Companies with Committees'), the majority of which consists of independent directors, and then clarify and disclose the basic approach and procedures concerning such selection/nomination of CEO and other key executives. Especially with regard to the CEO, it is important to disclose the reasons for selection as well as expected qualifications and roles.**

Furthermore, all directors should be subject to election by the general shareholders' meeting every year.

2. Responsibilities of the Board of Directors

(1) Roles and Responsibilities of the Board of Directors

The fundamental target of the Corporate Governance Code is to create an environment where listed companies in Japan can increase their 'earning power' (in terms of both growth and profitability) on a long-term and sustainable basis. Accordingly, the content of the Code should place more emphasis on 'offensive governance' to increase growth and profitability of the companies, not only on 'defensive governance' to reinforce compliance. Therefore, **the Code should stipulate that the roles and responsibilities of the Board of Directors include the monitoring of 'offensive governance', more specifically, monitoring of whether or not the management functions well for long-term sustainable increase of corporate value.**

As far as 'offensive governance' is concerned, the most important exercise of authority would be the exercise of authority over personnel issues (specifically, decisions on selection/dismissal and remunerations). In 'offensive governance', it is essential to incentivize management to increase long-term growth and profitability of the company through the exercise of authority to decide such selection/dismissal and remunerations in a timely and appropriate manner. The Code, therefore, should stipulate that **the key roles and responsibilities of the Board of Directors are to select/dismiss CEO and other key executives, as well as to incentivize them to work with appropriate entrepreneur spirit.**

Considering such roles and responsibilities of the Board of Directors, the formulation of succession plans for the CEO and other key executives as well as the criteria and procedures to appoint CEO and other key executives should be clearly defined, implemented, and monitored by a nomination committee which is proven to be independent. As this approach has not yet taken root in Japanese companies, the Financial Services Agency (FSA) and Tokyo Stock Exchange (TSE) should consider the publication of good examples, which are as illustrative as possible so that companies

can smoothly respond to the enforcement of the Code.

Meanwhile, the companies are required to implement the PDCA cycle steadily, which is fundamental to facilitating their growth and profitability. Accordingly, the Board of Directors should not only guide broad corporate strategies, but also oversee whether or not CHECK and ACT steps in the business execution cycle are working adequately. In this sense, the Board of Directors is expected to play an active role in assessing/monitoring management.

(2) The Separation of Execution and Supervision Functions

The separation of execution and supervision functions is essential for 'offensive governance' in terms of improving both the quality and speed of managerial judgment. Furthermore, the Code should clearly articulate expected roles and responsibilities of the Board of Directors in association with the separation of execution and supervision functions. Especially, **in many cases, 'the execution of important operations', which is the matter subject to the Board of Directors' resolution is defined too broadly.** The Board of Directors is expected to have meaningful discussions about crucial matters and make decisions, rather than taking care of all kinds of matters. Accordingly, **to make supervision and monitoring functions of the Board of Directors more effective, companies other than 'Companies with Committees' should also limit the matters subject to the resolution by the Board of Directors to the possible extent permitted by the Companies Act.** In the meantime, the roles and responsibilities of executive officers should also be clarified in a similar manner.

(3) Diversity

Due to the Japanese style of management characterized by seniority-based promotion and lifetime employment, members of the Board of Directors and top management of Japanese companies tend to be homogeneous. Therefore, it is a key challenge for Japanese companies to consider ensuring the diversity of the members of the Board of Directors and top management. Currently, the low female ratio receives a lot of attention, but the problem is not limited to this area. In terms of ensuring diversity, Japanese companies are also behind in the following areas: promotion is typically from within the company; many members of top management do not have experience of working for other companies; and there are few foreign nationals in top management. Accordingly, **we should facilitate ensuring diversity in gender, age, nationality, skills, background in order for Japanese companies to challenge the status quo and regain earning power.**

(4) Fiduciary Duty

Listed companies raise funds broadly from general shareholders, and manage such funds in the form of business operations. Thus, they have a fiduciary duty similar to institutional investors. The Board of Directors should, therefore, make efforts to increase the shareholders' medium to long-term return on investment.

The reinforcement of the investment chain, where companies make profits through medium to long-term value creation and pass such profits on to the household sector,

directly leads to the national wealth creation as well as the virtuous cycle of the Japanese economy. The Code should stipulate that listed companies and their directors have significant responsibilities for the advancement of this investment chain.

(5) Director's Access to Information

Corporate governance issues for Japanese companies are not only centered around preventing reckless decisions and actions by CEO who hold absolute control, but also lie in the situation where inconvenient decision-making is postponed due to maintaining internal harmony among homogeneous directors. In such situations, **it is important to make use of independent directors, who are not involved in conflict of interests within the company, and thus able to destroy harmony, not needing to be overly sensitive to the situation.**

Consequently, it is essential to ensure the independent directors have access to information necessary to fulfill their responsibilities, and supporting systems are in place.

3. Company Auditors/The Board of Company Auditors

In the Japanese Corporate Governance Code, it is appropriate to refer to company auditors and the board of Company Auditors, which is a distinguishing feature of Japanese-style governance. Yet company auditors do not have voting rights, and thus do not have the right to be involved in the final decision-making on nominations and remunerations, which is the essence of 'offensive governance'. Given this, **the Code should clearly stipulate that the presence of (outside) company auditors cannot be an alternative to independent directors.**

On the other hand, **the Code should also clarify that the core function expected of company auditors is 'defensive governance'.** Recently, even after the implementation of "J-SOX", 'defensive governance' including company auditors has not sufficiently fulfilled its responsibilities, as non-compliance cases involving top management, such as large-scale window-dressing still exists. Accordingly, **to prevent such significant scandals involving top management, it is essential to make the company auditors' functions more effective in order to reinforce 'defensive governance'.**

Specifically, **company auditors are in a position to decisively prevent misconduct even if they must challenge the CEO in emergency situations. Thus, it is necessary to establish a mechanism under which candidates for company auditors are not appointed in compliance with the CEO's wish.** To be more specific, the nomination committee, the majority of which are independent directors, should play a major role also in the selection of company auditors. It is also necessary to establish objective criteria for nomination/selection, and develop proposals for the election of company auditors by the committee, so that neutral and independent company auditors are elected.

In particular, full-time company auditors are in a position to easily obtain information necessary for auditing, and therefore are key players in the Board of Company Auditors.

Accordingly, **to ensure that they execute their duties neutrally and independently, the companies should introduce a system where outside company auditors work full-time.** If such full-time company auditors were involved in the execution of the company's operations in the past, the company must reasonably explain that they can execute their duties neutrally and independently.

4. Dialogue with Shareholders

(1) Establishment of the System

CEO and Chief Financial Officer (CFO) are primarily responsible for supervising overall dialogue with shareholders and realizing constructive dialogue. They should actively have dialogue with shareholders, and also make arrangements to keep all the members of the Board of Directors informed of shareholders' interests.

In addition, other board members, especially independent directors, should also play an important role in dialogue with shareholders. Their commitment is required: for example, they are expected to attend meetings with shareholders upon request.

(2) Disclosure of Targets Related to Capital Productivity

Since the burst of the economic bubble, capital productivity of Japanese companies has remained significantly lower than that of US/European companies for a long time.

Higher capital productivity not only increases profit distribution to shareholders, but also secures resources for investment to improve competitiveness of companies, thus leading to the growth of the Japanese economy. Moreover, an increase in profit distribution to shareholders also contributes to national wealth generation and economic growth as a result of advancing the investment chain.

Accordingly, **to increase their capital productivity, companies should set and disclose management indicators with targets. For such target-setting, the companies should use their global competitors as a benchmark. In case where such a management indicator is the return on equity (ROE), the target should be at least 10%.**

END

日本取締役協会 Japan Association of Corporate Directors

協会について

委員会・セミナー

報告書・NEWS

会員募集

サイト内検索

組織概要

◆日本取締役協会の組織機関

*敬称略 2014年7月15日

現在

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| 設立 | 2002年4月1日 有限責任中間法人 日本取締役協会として登記 | |
| | 2009年1月21日 一般社団法人 日本取締役協会に登記変更 | |
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| | 企業経営と会計委員会 | 新井純（昭和シェル石油顧問） |
| | 独立取締役委員会 | 富山和彦 |
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| | 成長戦略委員会—持続的成長をもたらす経営力とは | 松井忠三 |
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| | 会社法制委員会 | |
| | 不確実な国際環境変化と企業経営委員会 | 東哲郎、清水雄輔（キッツ名誉最高顧問） |
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| 事務総長 | 林部健治 | |
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よくある質問

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アクセス情報

会員募集

協会年間スケジュール(2014年度)

PDF member

協会 2013~2014 年度活動概要

PDF member