Corporate Governance in Groups of Companies:
A Perspective of Corporate Law and Securities Regulation

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Hideki Kanda
University of Tokyo
Corporate Groups in Japan: Type 1
Corporate Groups in Japan: Type 1a

Listed Companies

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Corporate Groups in Japan : Type 2

Listed Companies
Corporate Groups in Japan: Type 3

Listed Company

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Problems in Corporate Law and Securities Regulation

• Agency Problems
  – Managers/Directors versus Shareholders
  – Majority (or Controlling) Shareholders versus Minority Shareholders
  – Managers/Shareholders versus Other Constituencies (such as Creditors)
Responses in Corporate Law and Securities Regulation

- **Responses**
  - Disclosure
    - financial reporting on a consolidated basis
    - disclosure of intra-group transactions
    - disclosure of ownership structure
  - Ex Ante Rules
    - equal treatment of shareholders
  - Ex Post Standards
    - fiduciary duty
  - Other
Theme 1-1: A group structure may aggravate agency problems: a simple example
Theme 1-2: A group structure may aggravate agency problems: a holding company example
A Real Example for Theme 1-2: A group structure may aggravate agency problems

- UFJ Bank
  - UFJ Holding
    - shareholders
    - managers
    - listed company
  - 100% control
  - no control
  - adoption of poison pill by charter amendment
  - competing bid

- SMBC
- BOTM
Theme 2: A group may pursue the interest of the group, not the interest of the individual company.
A Real Example for Theme 2: A group may pursue the interest of the group, not the interest of the individual company

- Mr. T
  - Kokudo (manager/controlling shareholder)
    - Seibu Railways (listed on Tokyo Stock Exchange)
  - not listed
  - minority or public shareholders

Seibu
Kokudo
Mr. T

not listed
minority or public shareholders

listed on Tokyo Stock Exchange
Pattern 1-1: A group structure may aggravate agency problems: a simple example

Traditional legal approach seems to work with some modification.

Japanese law:
(1) disclosure [expanded in 2005], (2) exchange rule on listed subsidiaries, and (3) extension of traditional rules in corporate law
Pattern 1-2: A group structure may aggravate agency problems: a holding company example

Traditional legal approach seems to work with some modification.

Japanese law:
(1) disclosure, and (2) extension of traditional rules in corporate law
Pattern 2: A group may pursue the interest of the group, not the interest of the individual company.

Query: Can S's manager maximize the value of the group?

German approach:
Legally recognize an entity

Sometimes listed, sometimes not listed

Manager/majority shareholder

Minority shareholders

Listed
Fundamental Problem in Law's Recognizing a Group as One Entity

• There are a variety of groups.
• It is difficult to define a group and apply "rules and standards" provided by traditional corporate law.
• As a result, any attempt to define a group and regulate it may lead to being over-inclusive or under-inclusive.
Scope of Consolidation and Group

- consolidation for financial reporting
- group definition?
- group definition?
Pattern 2: A group may pursue the interest of the group, not the interest of the individual company.

Query: Can S's manager maximize the value of the group?

Japanese law:
(1) disclosure [expanded in 2005], (2) exchange rule on listed subsidiaries, and (3) corporate law (rule is unclear)
An addendum: rethinking listed subsidiaries hostile takeover battles and the market for corporate control in Japan

manager/controlling shareholder, but with only 10%

hostile takeover attempt

public shareholders

listed
Conclusion

• Disclosure
  – Disclosure is helpful.
  – Disclosure delegates the solution to the market place.
  – For disclosure to work, proper infrastructure is important.

• Rules and Standards
  – Pattern 1 seems relatively easy.
  – Pattern 2 seems more difficult.

• How can we regulate an entity which the law does not recognize?