



## **The Second Asian Roundtable on Corporate Governance**

### ***The Role of Disclosure in Strengthening Corporate Governance and Accountability***

## **TSE Efforts to Encourage Thorough Corporate Governance by Listed Companies in Japan (May 2000) Tokyo Stock Exchange**

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### **1 Corporate Governance & TSE Involvement**

Corporate governance discussions deal with a wide-range of topics, including accountability to shareholders, disclosure to stakeholders, prevention of legal infractions, structure of corporate decision-making, and other matters relating to greater management efficiency and the establishment of a corporate philosophy.

There are two schools of thoughts surrounding corporate governance. One holds that a company's prime concern is to provide the largest possible profit to shareholders. The second holds that it should also balance the differing needs of stakeholders. Regardless, corporate governance will undoubtedly lead to a reassessment of the role and importance of shareholders/investors here in Japan, where historically shareholders have been sidelined.

The establishment of a corporate philosophy is sure to lead to improved quality of listed companies.

Given these points, TSE believes it is important to take as active a role as possible in encouraging corporate governance by listed companies.

### **2 Underlying Philosophy of Measures**

Discussions of corporate governance have only just started in Japan, and as yet there is no consensus as to which model Japanese companies should follow. A number of proposals have been put forward, each with its

supporters and critics. As TSE has so far not been directly involved with any of these proposals, it is difficult for TSE to put its support behind any of them.

Further, although many listed companies are debating measures to be taken, only a few have actually taken any action. As any measures implemented by these companies are only recent, it is too soon to be able to assess their efficiency and effects.

Thus, there is a risk that if TSE imposes a framework and standards while companies are still gearing up to deal with corporate governance, these companies may consider that all that is needed is simply to abide by this framework. This may prevent companies from actively implementing their own better policies.

Thus, TSE considers it of prime importance to raise awareness of corporate governance, and to create an environment where listed companies will deliberate on and implement their own policies. It is still premature for TSE to take any decisive action such as expressing support for, and calling for compliance with, any existing proposals such as the principles of JCGF, the Japan Corporate Governance Forum, a body created by economic leaders in 1994 to study corporate governance. The forum suggested 17 principles of corporate governance to the public, but TSE had not been involved in the discussions of these principles. TSE also considers it premature to include corporate activity guidelines for companies to comply with, or standards for a company's governing body, in its Listing Rules at this stage.

### **3. Measures Taken by TSE**

Currently TSE is following two courses of actions: (1) requesting disclosure of management policies and the status of corporate governance in companies' preliminary financial results, and (2) education and support through lectures and publications. Prior to these actions, TSE conducted a survey on corporate attitudes towards corporate governance.

#### **(1) Survey**

TSE conducted a survey in September 1998 of all listed companies concerning their interest in, and attitudes towards, improving corporate governance practices. The survey found quite a high level of interest in the recent discussions on corporate governance, though one third of the total listed companies did not answer the questionnaire. Companies' interest was not focused on any particular issue, but rather included such matters as auditor issues, board of directors, prevention of legal offences by companies, and accountability to shareholders.

More than 70% of respondents had increased the number of external auditors to half of the total, and 80% had elected independent and neutral individuals as auditors. Around 30% companies had already elected external board members and reduced the number of board members. More than 40% of the companies had started discussing improved accountability

to shareholders at the general meeting.

Nonetheless, only 30% had discussed implementation of any measures to strengthen the function of auditors. Most of the companies proved to be still in the early stages of discussions concerning the introduction of executive officers, realising clearer remuneration packages, establishing a body to prevent legal offences, establishing an external body to advise management.

After all, it can be said in general that Japanese companies are on the stage of groping for their right corporate governance style.

## **(2) Call for Inclusion of Corporate Governance Information in Preliminary Financial Results (31 March 1999)**

TSE requested all the listed companies to include a statement of their attitudes and actions taken to improve corporate governance, and any results in their preliminary financial results. A letter was sent from the TSE President to company representatives requesting their cooperation with implementing corporate governance.

### **(i) Details**

Qualitative information is asked for under 'Management Policy' and 'Management Results', instead of the former 'Business Results for Current & Next Period' and 'Dividend Policy', in the preliminary financial results.

### **(ii) Items**

#### **Management Policy**

In addition to the details of basic management policies, including management goals, role of shareholders/investors in management and basic principles for distributing profits, it is requested to describe any management structural change to strengthen corporate governance. Appointment of external directors, establishment of remuneration committee, introduction of executive officer regime, and other items are to be covered. The descriptions should refer to the purposes, details of the measures, and what is expected as an effect of the measures.

#### **Management Results**

Details and analysis of business results for the current period, and forecasts for the next period, arising from the management policies stated above including those for corporate governance, should be described. Business results for the current period shall include details of profit distribution; and the factors underlying the forecast for the next period should be set out as well as the forecast itself.

### **(iii) Implementation**

The above has been in force since September 1999 for Preliminary Financial Results.

## **(2) Corporate Governance Symposium**

TSE held a symposium, titled 'Corporate Governance for Listed Companies –

Key Points & The Path Forward', on 29 July 1999. The purpose of the symposium was to provide support to listed companies in their efforts to implement corporate governance.

Attended by about 700, the symposium was opened by a keynote speech by Professor Hideki Kanda of Tokyo University Law Department. This was followed by a panel discussion, lead by moderator Mr Atsushi Suemura (Nippon Keizai Shimbun Editorial Committee), by Professor Kanda, Mr Nobuo Tateishi (President, Omron) and Mr Tadao Nishioka (Senior Managing Director, Nippon Life Insurance).

The panellists gave their opinions on the status of corporate governance in Japan, problems to be dealt with, reforms to the board of governors and auditor systems and the role of TSE in corporate governance.

The symposium was part of TSE's efforts to support companies pursue thorough corporate governance.

### **Major Points Raised at the Symposium**

- ⊙ Corporate governance based management is becoming increasingly important in Japan, as the financial/capital markets become increasingly globalised.
- ⊙ Corporate governance should not be legally imposed, but rather should be spontaneously implemented by companies.
- ⊙ The words executive director and independent director are bandied about, but these are only effective if introduced after consideration of the individual company's board of directors, and as appropriate to the company.
- ⊙ Some feel that, in light of the Liberal Democratic Party's (LDP) call for the reinforcement of the role of auditors, management audits should be carried out by auditors rather than by independent directors. Others suggest that companies where independent directors have an established auditing role should be allowed to opt out of using auditors.
- ⊙ Corporate governance has increased the importance of corporate disclosure. Corporate disclosure in Japan is radically improving, including amendments to the legal framework. Hopefully disclosure should become increasingly thorough with details given of management policies and strategies.
- ⊙ Japan is also seeing the emergence of a sense of fiduciary duty towards investors by institutional investors. Thus institutional investors too must become actively involved in corporate governance from the respect of fiduciary duty.
- ⊙ TSE should actively support listed companies' corporate governance efforts. Although nothing definite can be said now, possible actions could be the inclusion of corporate governance in our listing rules, the creation of a 'best practice' code, and the provision of information about individual companies' efforts.

### **(3) PR Publications**

#### **TSE Report (for listed companies)**

A series of articles were devoted to corporate governance in the TSE Report. The March 1999 issue carried results of the TSE survey on listed companies' actions toward corporate governance. The September 1999 issue reported the discussion at the TSE's symposium on corporate governance. TSE plans to carry, in the future issues, examples of actions taken by listed companies, examples of preliminary financial results that referred to corporate governance, and interviews with academics and other individuals.

#### **Lecture Digests**

Details of lectures at the symposium were published separately.

#### **Monthly Magazine**

A monthly TSE magazine 'Shoken' (meaning 'securities') carried an outline and details of disclosure requirements, details of lectures at the Symposium, and details of items for companies to include in the Preliminary Financial Results.

**President's Letter to Listed Companies**

31 March 1999

As you are aware there is any increasing awareness of the importance of corporate governance. Academic and industry leaders have debated and made recommendations about its value as a means of accountability to shareholders, and to check management practices and philosophy as well as efficiency.

Having always encouraged corporate management that takes into consideration investor and shareholder interests, TSE is extremely interested in developments in this area. 'TSE of the Future - Signposts to a New Stage' a recommendation report (10 February 1999) by the Securities Policy Committee, suggested an active involvement of TSE in the move toward thorough and active corporate governance by listed companies in light of providing investors with attractive investment products.

Against this background, TSE shall conduct activities to support improvement in corporate governance practices, as well as calling on listed companies to disclose the status of corporate governance within their companies including any future plans. In this and other ways, TSE plans to contribute to thorough corporate governance in Japan.

I take this opportunity to ask for your fullest cooperation with any TSE plans and policies concerning corporate governance.

Mitsuhide Yamaguchi  
President & CEO

## **Examples of Company's Disclosure on Corporate Governance Structure**

### **Teijin Ltd Co.- March 2000 Interim Report**

A strong management structure capable of withstanding change is indispensable in order to achieve continuous growth and development, in a global market undergoing swift and dynamic change. To achieve this calls for management to meet global standards, in other words to establish corporate governance and increase corporate competitive strength. To this end this company implemented fundamental management reforms in order to achieve improved transparency, preserve fairness and speedier decision-making in June.

#### **(1) Establishment of an Advisory Board**

An advisory board of knowledgeable individuals from Japan and overseas was established to give overall management advice and to evaluate the leadership.

#### **(2) Reform of Board of Directors & Introduction of Executive Officers**

In the interests of speeding up the decision-making process and to clarify responsibilities of execution, the board of directors was slimmed down to 9 from 24 members, and on the basis that a large slice of control would be handed over a system of executive officers was introduced.

#### **(3) Enhanced Auditing**

The company decided to appoint more than half of the total auditors from outside the company, and established a group audit committee from the auditors of the company and its major affiliates.

### **Tokyo Electron Ltd Co. - March 2000 Interim Report (Recipient of Disclosure Award)**

In the future we can expect the market to continue to grow ever larger, competition to become ever more fierce and our customers' business strategies to continue to diversify. Against this background, and in order for us to carry out truly global management, it is vital for us to establish a clear and easily comprehensible management structure where it can be easily identified where responsibility lies. In addition, as part of the globalisation of management, it is necessary for us to establish a

corporate governance framework and to delineate management which takes into great account the interests of shareholders. To this end we implemented an overhaul of the management structure in April 1998.

Firstly, the board of directors was realigned with its role defined as protecting shareholders' interests and optimising corporate value. The board is commissioned with the task of leading the company to long-term success and development. This is to be achieved by setting out basic management policies and determining business strategy, auditing business practice, evaluating and approving management results, assessing and recommending board members, and making decisions on any other matters called for under the Commercial Code. The board is also responsible for setting out management policies and auditing business execution within the global group.

Secondly, the corporate senior staff (CSS) system was established to take responsibility of proposing, deciding, and implementing business strategy to achieve results following the basic management policies determined by the board of directors.

Thirdly, the existing policies of quick decision-making, small operations and flat organisation are to be pushed even further. To achieve this the individual product business units have become the framework for a vertical management system straddling our group companies across the globe. In addition, sales and marketing departments have been established to oversee horizontal functioning between the business units.

Finally, a remuneration committee has been established within the board to determine the president's remuneration. The remuneration of the president and three other members of the board were disclosed in the sales report attached to the invitations for the 36th shareholders' meeting. A director has been appointed to see to the establishment of a comprehensive corporate ethics.

Our company is committed to corporate governance and continues to work to achieve and maintain transparent and objective management.