

# Contemporary Analysis of Japanese Corporate Boards

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## **Abstract**

*This paper evaluates the numerous sources about Japanese board of directors in the drastically changing business environment and thereby shows the road map of Japanese corporate boards. The results give in-depth understanding compared to the previous studies based on the evidence derived through the sub-samples representing different patterns of governance. Leader of the board of directors meeting is basically the president or chairman, especially in the companies having a traditional approach to corporate governance. Conversely, in case of the companies which have shifted to Anglo-Saxon committee system the leader of the board of directors meeting is mainly an outside director.*

*The jomu-kai (executive directors meeting) or keiei-iinkai (management executive committee) is still the center for major decisions in many companies having traditional governance system. The major decisions of global companies having either committee system or intermediate system are taken at the board of directors meeting. When attaining a long-term goal is uncertain, disregarding the nature of governance system, Japanese boards try to grasp any failure through their monitoring function. The larger companies having either intermediate or committee system shifted the power of selecting the next president from the existing president to a board committee. About half*

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*of the companies have already implemented the outside directors though some of them are not independent in actual terms. Particularly in larger companies having shifted to Anglo-Saxon committee system, there are independent directors similar to their Western counterparts. No matter the system is Japanese or Anglo-Saxon type, the board of directors and president or chairman of Japanese companies have an above average influence on their corporate governance systems. At present the companies have more concern about very specific board reforms such as implementation of performance evaluation and review of compensation. The 'ceremonial nature' of Japanese Corporate Boards has been shifting away to some extent and emphasizing more on efficient and effective decision making.*

*The nature and the role of board of directors of companies largely shifted to Anglo-Saxon committee system and intermediate system have been significantly changed. There is a trend of monitoring over execution indicating a tendency of converging toward the Anglo-Saxon model. Conversely, there are several larger companies greatly refusing to accept the new reforms, instead they consider improving the system along with the local and global requirements. The small and medium scale companies still prefer the traditional approach which benefits them over half a century. Historically, the Japanese people feel the obligation to a family, a company or country that leads to the consensus attitudes<sup>2</sup>. But they have taken some measures to improve their traditional system for better governance.*

**Key word :** *Board of Directors, Outside Directors, Executive Directors,  
Corporate Governance*

## **1. Background**

After World War II, Japan was one of the fastest growing economies in the world. The Japanese management system supported by friendly business-government relationship has achieved good performance<sup>3</sup> Many good Japanese companies pursued the growth-oriented strategies, preoccupied with actions of competitors, achieved the creation and ruthless exploitation of competitive advantages, and chose the corporate

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<sup>2</sup> Mallin (2004), p.175.

<sup>3</sup> Nakagaki (2004), p.3.

financial and personnel policies<sup>4</sup>. However, after the burst of the bubble economy, many Japanese companies have faced the restructuring of their businesses, which they had not experienced before. One of the specific features of Corporate Japan that commanded special attention was its corporate governance (CG) system based on *keiretsu*<sup>5</sup> which was exercised frequently by the Main Bank in the group and the system of cross-shareholdings. In accordance with many empirical studies, this CG system lead with main bank was one of the fundamental factors contributing to the success of Japanese economy especially from the period-of-high-growth to the period-of-second-oil-crisis (Chan-Lau, 2001). This view has been irritated by the collapse of the bubble economy in the early 1990s and the developments through the globalization and information technology revolution<sup>6</sup>. For example bank's ownership has decreased rapidly and declined to 7.6% in 2004. Also Administrative Reforms which had avoided private sector's fair competitions have promoted speedily<sup>7</sup>. Subsequently, various view points were emerged by giving multifaceted views and reasons to the problem. Among the widely known attempts, the slashing of interest rates to near zero percent (Nishiyama, 1999), substantial government expenditure on public projects (Cortazzi, 1999), deficit spending at unprecedented levels (Cortazzi, 1999) and several other motivational measures were taken to stimulate the Japanese economy.

In addition to uneven and ad hoc measures until mid 1990s, the Japanese government has already implemented two main systematic remedial approaches which make drastic changes even in the socio-economic system of Japan. The first one is the introduction of Japanese financial system reforms; "Japanese Big Bang" with the purpose of establishing a 'free, fair and global' financial system launched by Prime Minister Ryutaro Hashimoto's policy speech on 20th January 1997<sup>8</sup>. The scope of Big Bang is very broad reforms in capital markets, banking, insurance and the convergence of accounting standards toward the international level, including consolidated group financial statements (2000), market value basis on financial instruments (2001),

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4 Abegglen and Stalk, Jr. (1985), p.5.

5 An interdependent network of closely related companies, formally organizes around a bank (referred to as Main Bank) for their mutual benefit.

6 Nakagaki (2004), pp.7-20.

7 Ogino (2004), pp.63-68.

8 He stressed administrative reform, economic structure reform, financial system reform, social security reform, fiscal structure reform, and educational reform. Nakagaki (2003), p.27.

disclosure of pension account (2001), deferred tax accounting (2000)<sup>9</sup>, share-buyback program initiative (2001)<sup>10</sup>, basket expense of R&D (1998) and so forth.

The next most significant reform effort is the revision of Commercial Law. More than one hundred years have passed since the Commercial Law of Japan was first introduced in 1899 during the *Meiji* era. Firstly many laws were drafted using the laws of various European countries including Germany, France, UK and USA as models. Even though the Commercial Law has been undergone a number of significant changes when and where necessary, particularly after World War II, further revision of many essential legal concepts and structures is now required to meet the reality of the socio-economic system of Japan in the 21st century. The revisions to the Commercial Law are numerous and wide ranging but can be categorized in to two main areas such as revisions relating to 'corporate structure & deal mechanics' and revisions relating to 'corporate governance' (Poe and Shimizu, 2002). According to Ministry of Justice (2004) the drastic changes in the area of CG include the introduction of Anglo-Saxon CG system with three committees and executive officer system, outside directors (majority of members of each committee should be composed of outside directors), delegation of substantial management authority, abolition of the restriction on the quantity of stock options and transfer of stock options, issuing new classes of shares with rights to appoint and dismiss a specified number of directors or statutory auditors, permission for "e-vote" etc.

Along with the above turbulent setup, Japanese corporate boards cannot be avoided from the impact evolved through the socio-economic changes affected by the globalization. The contents of Japanese corporate boards are gradually changing toward more suitable directions. For example many Japanese companies have decreased the number of corporate boards and have introduced the outside directors (see Table 1). On the other hand, most Japanese companies are sluggishly to a hybrid system that takes a base of traditional features and adds on to it some market- and shareholder-oriented practices<sup>11</sup>.

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9 Itoh (2005), p.3.

10 Nagano (2004), pp.201-202.

11 Jacoby (2005), p.77.

**Table 1 Corporate Boards of Japanese Companies  
(Listed companies on TSE 1st Section)**

	No.
1. Average size of corporate boards	10.5 person
2. Average no. of outside directors (in all listed companies)	0.6 person
3. No. of companies holding outside directors	525
4. Average no. of outside directors (in companies holding outside directors)	1.7 person
5. No. of companies having executive officer system	43
6. No. of companies having board of auditors system (traditional)	1,514
7. Average no. of directors in companies having board of auditors system	3.9 person
8. Average no. of outside directors in companies having board of auditors system	2.3 person
9. Average size of corporate board in companies having executive officer system	9.2 person
10. Average no. of outside directors in companies having executive officer system	4.2 person

Source: Seki (2005), p.39.

Data: Japan Investor Relations and Investor Support, Inc.

Note: No. of companies listed on the TSE 1 section at the end of March 2005 was 1678 (Tokyo Stock Exchange 2005a).

## 2. Research Objective

The purpose of the present study is to add some light on corporate boards which is a significant element of the Japanese corporate governance structure and is striving toward their ideals. More specifically, this study attempts to identify the nature and the role of board of directors (BOD) and thereby to reveal the reality and to understand the future path of Japanese corporate boards.

## 3. Review of Literature

The literature on Japanese BOD is very few and the depth of the studies is also a significant matter to be concerned. The only available empirical studies on Japanese boards and their roles are also highly influenced by the economics-based interpretations and basically the argument is that the period of rapid industrialization subsequent to the *Meiji* restoration was fundamental in the way that Japanese boards developed. According to Fruin (1992) the former *bushi*<sup>12</sup> or samurai who originally controlled commerce and the

<sup>12</sup> Nitobe described that *bushi* must sustain the code of moral principles, possessing all the powerful sanction of veritable deed and of the fleshy tablets of the hearts. Nitobe (1998), pp. 33-35.

merchants suddenly understood that they did not have adequate knowledge and skills to run the new businesses evolved through rapid industrialization and growth. As evidenced by Yonekawa and Yoshihara (1987), former controllers of commerce were willing to rely on the fresh knowledge and experience of new graduates from the university and experienced business handlers from the West in order to run the organizations initiated by them. Hence there was a bloom of taking decisions by the professionals like supervisors, bookkeepers in place of technical owners. In the other words, in *Meiji* era, former bushi entrepreneur and newly established entrepreneur have led the modern Japanese company system<sup>13</sup>.

In a similar way, even though BOD was presumed to be a body of representatives of shareholders in the Japanese Commercial Law it became a representative organ of employee interest rather than a representative of shareholder interest. This nature was rapidly developed to appoint members to the board exclusively from the layers of employees and the board was not any more toward the shareholders instead it was transforming to a center of safeguarding the employee rights and interests. The tendency was further confirmed by Yui (1984), mentioning that the extraordinary and persistent pace of economic and technological developments in Japan has further concentrated power into the hands of top executives.

Accordingly, as a whole, it seems that there is a common belief that the board is a representative body of employees instead of shareholders. Is it reasonable to generalize the concentration of Japanese board which is having number of levels of directors in the top level in such a manner? However, in relation to a recent finding, Itoh and Teruyama (1998), opening the black box of top management in Japan, explain the different attitudes and behaviors between the different layers of directors within the board. Along with their findings, senior directors are more concern on investors and share prices while non-titled directors have a propensity to focus highly on employees, specifically those who are in the operational areas which they represent. In large companies, statutory auditor also tends to be focused on the welfare of investors and employees as well, though in smaller firm's auditors have a tendency to concern with loyalty to the company and cooperation with senior directors. External directors tend to focus on stock prices and credibility of the company on the side of shareholders and banks, and are far away from concerning about the employees.

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13 Takahashi (1977), pp. 20-22.

As the leadership engine of the company, the board's function is to set the company's strategic direction; vision, mission and objectives and to ensure that they are achieved. Corporate governance guideline, policy and code provide the necessary framework that will back the board to meet the expectations or the rational of the company, however, it is up to the leadership function of the board to drive toward the overall prosperity. According to Carver John (2002) author of Policy Governance Model, direction is the job of the board to set the ends, that is to say, to define what the company is in business for. There are apparently dramatic board changes including the area of board's leadership and direction role under way in Japan. In a recent study Learmount (2002) found no evidence of operational decision-making being decentralized, or the powers of the board being revised in any significant way. Fujishima (2005) insists that *Shacho* (presidents) of Japanese companies have been holding the strong powers in critical decision making from corporate strategies to day-to-day decision making<sup>14</sup>. Further BOD as a group was described as little more than a ceremonial body, with no real authority of its own. More specifically, the board did not have any input into the generation or revision of major decisions as such decisions are taken by a powerful small group of senior directors (most of time referred to as *jomu-ka*) in a separate meeting instead of the board meeting. The situation is more critical when the company is a family or a private business. As quoted by Learmount (2002) from his interview findings 'My husband and I talk about the strategy and policies we are thinking about in the long and medium-term, and the board will decide whether they should say something or agree or whatever...'. Hence, there is a question whether the leadership and direction role is played by all the members of the board as a whole or a restricted group of senior directors and as a result, the strategic direction of the company is not determined by the contribution of all the members of the board.

As far as the views of CalPERS (2004) and OECD (1996) on the role and the practices of Japanese BOD are concerned, Japan's boards need to improve their accountability to shareholders and the most feasible way of achieving this is to increase the number of independent directors. Well-known institutional shareholders such as CalPERS have established specific guidelines relating to Japanese boards within their principles for good governance in Japan as follows; 'Japanese Corporate Boards Should Consider the Interests of, and Strive for Accountability Toward, All

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14 Fujishima (2005), pp.18-19.

Shareholders...Corporate Boards Should Include Directors Who are Truly Independent from the Corporation and its Affiliates...Best Governance Practices in Japan Should Include Elements that Strengthen Management Accountability to Corporate Owners through the Director-Shareholder Relationship'. (CaIPERS, 2004).

In view of that, when a board is composed mainly of insiders, as is typically the case in Japan; it must take particular concern to avoid any conflict of interest and to focus on the interests of minority shareholders. The board's preliminary attention should be on safeguarding the interests of shareholders and providing them with the highest possible long-term returns on their investment ensuring that a board of director's major concern is to represent all of a company's shareholders. During the last two decades, it is observed that there were a considerable number of external directors being appointed. OECD (1996) evidences that approximately 25% of Japanese company directors do come from outside.

However, it is a puzzling issue whether the Japan's external directors are independent in real terms, because most of these external directors come from related organizations such as other companies or banks. A noteworthy observation is that little below 40% of the outside directors (see Table 2) are coming either from the company's parent company, group company or main bank generating a significant issue relating to the independence of outside directors. Directors from client or trading companies means

**Table 2**

<b>Outside Directors</b>	<b>% of Responded Companies</b>
1. Group companies	17.7
2. Holding companies	16.0
3. Main bank	4.6
4. Other banks	1.7
5. Client	29.8
6. Friendly companies	8.8
7. Insurance companies	3.9
8. Consultants and lawyers	3.4
9. Bureaucrats	1.1
10. Others	13.0
Total	100

Source: Dissa Bandara (2004) based on the Policy Research Institute of Ministry of Economy & Financial Services (2003).



that they are from the *keiretsu* companies which again a destructive factor of their independence showing an aspect of the traditional governance system.

Therefore, it is quite straightforward to understand that Japan's external directors unable to exercise independent opinion or represent the shareholder interest. This may be the reason for CalPERS, (2004) to suggest that the Japanese boards should include independent directors to ensure that all shareholders are well represented, particularly in cases where executive directors may have conflicts of interest. Independent directors provide additional assurances to outside investors that a company is run in accordance with the law and with sound accounting and auditing principles. To the extent that independent directors cause a corporation to focus less on the interests of insiders and more on shareholder returns.

Viner (1993) in his viewpoint argues that the malfunctioning of accountability is considerably due to the inadequate independent supervision. The fundamental authority of the BOD of Japanese companies has traditionally lain in the board's power to prescribe the business practices to be executed and to monitor the company's directors and corporate executives in the execution of their duties. Specifically, the BOD comprised of at least three board members elected at the general meeting has the authority and the obligation to determine corporate policy regarding business execution and to elect a representative director, who is authorized to execute these decisions, while also monitoring the representative director and the executive directors in the performance of their duties. In the West the accountability of the board is guaranteed due to the considerable number of independent directors and their dedicated work. Viner specifically mentions that "the ability of the president to collude with the directors who are themselves senior managers appointed by him in order to conceal serious irregularities, is particularly strong in Japan where the absence of any outside supervision provides a cloak for every dragger". Accordingly, the president becomes the most powerful figure and has the power to appoint or and remove directors in practice as he wish. Hence, the other directors or and officers become unnecessarily obedient to the president.

By looking at the Japanese boards and the contents, an outsider may presume such a view and might feel the hypothesis is logical. However, Viner's view is some what ambiguous, may be due to some limitations of his inquiry in to the practice of Japanese boards. Though he criticizes the tradition of appointing the directors to the Japanese board by the president, the real world situation, in general, in the West except countries

like Germany and few other Asian countries, the appointment is done by based on the invitation of the president or CEO. In addition, when compared to WorldCom and Enron cases in the US, it is rear such material irregularities or misstatements in the Japanese setup. As mentioned by OECD (1996), compared to the UK and US, it is easier for shareholders to nominate candidates to the Japanese board and to dismiss them. As an example, according to the article 257 of Commercial Law, a motion to dismiss a director can be filed by a shareholder controlling 3% of the issued shares. Further the cost of suing the directors had also been remarkably reduced by the amendment to the Commercial Law in 1993<sup>15</sup>. Except for the over emphasized statement of Viner, the essence of his argument is relating to accountability of Japanese BOD. On average, in the Japanese setup most directors had worked for the company as employees or managers in their career ladder. Therefore, as a result of the 'life time employment system' and the 'seniority system', the directors are officers as well as BOD. Hence there is no proper monitoring over execution since there is no demarcation except the labels 'officer' and 'BOD'.

Relating to the above but not adhering to the same, another argument is that the conventional board members lack an overall understanding on corporate management. As Yanai (2003) evidences, although these directors attend board meetings as representatives of their specific departments, they lack a company-wide perspective on management. In contrast with the Anglo-Saxon system, the individual director of the board is a functional head of the organization. Therefore, naturally each board member specializes only for his or her own specific field rather than having an organization-wide management perspective. Furthermore, with all members of the board in positions subordinate to the president as mentioned above and these boards of directors were criticized for not fulfilling their obligation to monitor the president. Until the 'corporate executive officer system' introduced by the revised Commercial Law in 2002, there was

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15 This revision to the Commercial Law article 267 (5) reduced the revenue stamp duty (8,200 yen) by introducing the calculation based on an estimated stable fine, even though the actual figures may be significantly varied. This is a considerable reduction of cost of suing a director by a shareholder compared to the amount to be incurred for such action before 1993. However, Japan Business Federation asked to set a cap on the amount of damages on company executives. And *Corporate Governance Manual* edited by Japan Association of Corporate Executives recommends bearing the burden by the company against a shareholder law suits in order to maintain excellent directors (2005), p.170.

no incentive to separate monitoring from execution in Japanese firms.

## 4. Methodology

Since the issues of Corporate Governance about the Japanese Companies are focused recently, gathering the data is very difficult. However, to the research conclusions to test subjective beliefs against objective reality and have the findings open to further scrutiny and testing<sup>16</sup>, we must get the available data as possible as we can.

### 4.1 Data Collection

For the purpose of doing the research 120 companies were chosen at random, based on the companies listed on the first section of the Tokyo Stock Exchange (TSE)<sup>17</sup>. Having a response rate of 52.5%, 63 companies had responded covering 25 out of 33 officially classified sectors of the TSE (Tokyo Stock Exchange, 2004). In addition another 15 small and medium scale companies (SMCs) were also selected randomly to the sample. When selecting a company, a reasonable care had been exercised to include the companies with respondents with a considerable understanding about the keywords such as CG, IR activities, role of BOD, disclosure requirements and annual reporting.

The respondents include popular global companies, leading companies, medium and small scale companies in various kinds of industries. The time period covered by the study is 5 years from 1999 to 2004 giving special reference to the corporate governance situation prevailing at the financial year 2003/2004. A variety of data was collected including governance related data such as frequency and timing of board meetings, circulation of proceedings, way of decision making, implementation of new systems, performance evaluation of boards, future actions to be taken for a stronger board etc. and some financial data. There were several data collection methods adopted with a view to obtain a more valid and comprehensive data set considering the limitations of obtaining such corporate data. Firstly, a questionnaire survey was conducted in May and June 2004 distributing the survey sheets through postal mail, e-mail and facsimile. After reviewing the responses, 10 companies were selected representing all the kinds of

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16 Cooper and Emory (1995), p.10.

17 At the end of December 2004, number of the listed companies in TSE was 2,276 (1595 1<sup>st</sup> section companies) Tokyo Stock Exchange (2005b), p.103.

companies for adopting critical incident technique suggested by, Chell (1993) using both 'front door approach' and 'back door approach'. Further, telephone interviews were conducted in 30 companies for further clarifications. In addition, many other secondary sources such as press releases, homepage disclosures, annual reports, IR reports, management reports, corporate plans etc. were used as supplementary data.

The data were analyzed by using both qualitative and quantitative techniques. Since there can be several corporate governance systems as a result of the recent reform efforts, the companies in the sample were categorized mainly into four test categories for the purpose of discussing the results of the critical incidents as follows.

- i. Small and medium scale companies (basically having a traditional governance system)
- ii. Larger companies having traditional governance system
- iii. Larger companies having intermediate governance system
- iv. Larger companies having Anglo-Saxon committee system

#### **4.2 Corporate Governance Characteristics of Responded Companies**

According to the survey conducted by the Authors in 2004 majority (67%) of the respondents are willing to label their CG system as 'Traditional Japanese System'. Only 8 companies (13%) has shifted to the newly introduced 'committee system' suggested by the amendments to the Commercial Law in 2002 and the rest (21%) wishes to label their system as 'intermediate system'.

Though it is too early to evaluate the recent reform efforts, it is clear that there is a considerable change occurring within the corporate governance setup of Japanese companies. Table 3 gives evidence about a number of sub-systems introduced during the last few years. Among the newly implemented systems, outside auditor system is not completely a new experience for Japanese companies as it was a legal requirement from the first half of 1990s. The outside director system was also in practice in some of the companies from early 1990s as a voluntary reform tool. However during the last 5 years the implementation of various systems by the respondents had been accelerated at an increasing rate.

**Table 3**

Unit: %

<b>Sub-Systems introduced during the last 5 years</b>	Outside Director System	Outside Auditor System	Executive Officer System	Stock Options System	IR Activities
1. More than 5 years ago	35	75	11	10	73
2. During the last 5 years	17	19	50	38	22
3. From now on	3	0	0	2	0
4. Not interested	10	2	5	10	0
5. Not decided yet	30	2	24	34	0
6. No Response	5	3	10	5	5
Total	100	100	100	100	100

Source: Survey Conducted by the Authors in 2004.

## 5. Empirical Results

As one of the latest surveys, this study found important and interesting empirical evidences covering many aspects of Japanese corporate boards. The following analysis of results reveal more about frequency and timing of board meetings, circulation of proceedings, way of decision making, implementation of new systems, performance evaluation of boards, future actions to be taken for a stronger board and so on.

### 5.1 Leader of the BOD Meeting

One of the key areas of the study is to identify the nature of board meeting and the leader of the BOD meeting. As per the Table 4, in 44% of the companies, chairman becomes the head of the BOD meeting. This is a favorable trend growing within the Japanese companies indicating a substantial relief from the pressure of execution on monitoring. However, still in 48% of the companies, president becomes the head of the BOD meeting while acting as the CEO of the entity. This shows that about a half of Japanese companies has still lack of separation between monitoring and execution or in other words there is a considerable influence from the president on the board functions. Only 4 companies of the sample having either Anglo-Saxon committee system or intermediate system are using a different way and the head of the BOD meeting is an outside director indicating more independent leadership for proper monitoring.

Table 4

Who is the leader of the BOD meeting?	No. of Responded Companies	%
1. President	30	48
2. Chairman	28	44
3. Others	4	6
4. No response	1	2
Total	63	100

Source: Survey Conducted by the Authors in 2004.

In coincide with the above findings, the critical studies found more specific evidences about the head of the BOD meeting. The smaller companies addict to the traditional system and the president plays one man show. As a result he becomes the head of the BOD meeting too. This nature is mainly due to less number of directors/managers, lack of leadership ability with higher educational setting and lack of resources. These things concentrate everything in the hands of the person who has been appointed as the president. One president of a smaller company spoke; "Ours is little bigger than a kind of *sakanaya-san* (a mom-and-pop store). So we have limited resources, market and managers. All directors have climbed through the seniority system. Though I like, there is no person to take responsibility other than *gambaru* (indicates working hard for the given target) with employees. Their contribution to long-term decisions is very unsatisfactory. Therefore, I am like the father of Japanese *ie* (Japanese style family)".

The evidence grasped from several other medium and small scale companies also repeatedly confirmed the above tendency using similar explanations. The dominance by the president in every matter is not an automatic function rather it evolves through above circumstances. Then the president becomes the father of the house engaging with any activity for the benefit of all family members (corporate paternalism). As the company is also a social unit it automatically utilizes the cultural values evolved through years and years<sup>18</sup>.

As far as the larger companies having traditional governance system are concerned, they also use a similar system giving similar reasons except the limited

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18 In case of Japanese companies, the followers tend to follow the leaders (effective executives) who have human characters. Nakagaki (2003), pp.20-22.

resources including human resource. It seems that every one in the family (here the company) respect the father (here the president) and expect everything from him. One senior managing director emphasized; "Though.....(name of their company) is seeking for profits (for all), this operates like a family. This is a real Japanese style family. The status for father, mother and children is determined. Therefore, father is powerful to make any decision. It is not bad. As the environment is changing, recently all other members help him to make better decisions to face the competition".

The *ie* concept is a deeply routed social value even inside a company. Therefore it is an inherent feature of governance in the Japanese company, especially having a traditional approach to CG. Conversely, the companies which converted their governance system to Anglo-Saxon committee system do not seem to be adhered to such traditional matters; instead they pursue the rules and norms which followed by the system. Therefore the leader of the BOD meeting is mainly an outside director like in the US current practice.

## 5.2 Timing of Circulating the Proceedings

As a basis for a proper board meeting the notice, the agenda of the meeting is a must. On average, Japanese companies tend to use the term 'proceedings' or in other words all the above materials are sent together for inviting to the next meeting. According to Table 5, 38% of the companies circulate the proceedings one or two weeks before the BOD meeting allowing the members to prepare for the meeting adequately. On the other hand 44% of the companies do not have a specific time period to circulate the proceedings. This means that there is an uncertainty about giving a sufficient time for

**Table 5**

<b>When do You Circulate the Proceedings of the Board Meeting?</b>	<b>No. of Responded Companies</b>	<b>%</b>
1. One or two week before the next boards meeting	24	38
2. The day before the next board meeting	3	5
3. At the time of Board meeting itself	2	3
4. No specific time period	28	44
5. Others	2	3
6. No response	4	6
Total	63	100

Source: Survey Conducted by the Authors in 2004.

preparation for the board meeting in little less than a half of the companies. Only three companies (5%) distribute the materials just one day before the board meeting laying the directors in a harder situation to get prepared overnight for the meeting.

As far as the critical incidents are concerned, almost all the participants declared that they distribute at least a brief notice. Sometimes 'others' contains important issues compared to listed items in the notice or agenda. Timing of distributing the materials is not certain; it ranges from one or two days to one or two weeks. Intermittently, there are some instances where there is no proper notice in advance, for example emergency issues to be attended. One senior managing director of a medium scale company contributed; "we get a notice from the office few days before the meeting (some times 1 week, but mainly few days before and sometimes suddenly when there are hot issues with CEO), occasionally with reports. For me, the most important things are the matters discussed under 'other' though they are not printed. Of course, points listed on the notice also important..."

In larger companies, whatever the governance system is; a formal notice with proceedings is sent at least one week before the meeting and as a minimum, one meeting is held once a month. The number of meeting for a month is not restricted or predetermined; when and where necessary additional meetings are called to address the important matters immediately. A director of a company newly shifted to intermediate governance structure added; "under the new setting we get the materials (defined in the manual) around 1st as we have the meeting around 10th every month. Additional meetings are held when required. Now the arrangements are better for the meeting...(silence) ..may be due to outside directors..."

Companies are gradually entering to circulate a more formal set of proceedings with a notice at least a week before the next meeting even in several medium and small scale companies. However there are still a considerable amount of companies that do not distribute the documents allowing a specific time period before the meeting. Newly restructured companies toward Anglo-Saxon committee system or intermediate system attempt to provide a comprehensive set of materials at least one week before the meeting.

### **5.3 Major Decisions**

Theoretically the board of directors is elected by the owners to owner's



interests<sup>19</sup>, the results say mainly the BOD is the body that makes major decisions of a company. According to DeMente (2004), Learmount (2002), Mizuo (2004), Monks (1994), Ohtsu and Imanari (2002), *jomu-kai* is the highest level decision making authority with limited number of managing directors. Conversely the results show that *jomu-kai* does not make any major decision in none of the companies of the sample, instead, as per the Table 6, in 87% of the companies the BOD makes all such important decisions. Another interesting point is that only 3% of the company presidents' make such major decisions which affect the future direction of the company. Based on the past literature, Mizuo (2004) pin points that the *shacho* (president) calls the shots on strategy, budget and nomination of other board members and officers. Probably this may be a recent development within the Japanese company with many other corporate reforms. The responses to the survey questionnaire seem to be an issue between '*honne*' (what one really feels) and '*tatemae*' (what should be done according the model)<sup>20</sup>. In Japan, so far there is no domestic market for top management<sup>21</sup>. Therefore, *shacho* (president) or *kaicho* (chairman) are usually promoted from the inside of the companies and has the strong power toward the company strategies.

Table 6

Who makes major decisions mostly at your company?	No. of Responded Companies	%
1. President	2	3
2. Chairman	0	0
3. BOD	55	87
4. Managing director meeting of the board ( <i>Jomu-kai</i> )	0	0
5. Corporate officer meeting	1	2
6. Others	5	8
Total	63	100

Source: Survey Conducted by the Authors in 2004.

#### 5.4 *Keiei-iinkai* Instead of *Jomu-kai*

However, closer investigations using specific case studies brought clearer picture about making major decisions in Japanese companies. Some respondents

19 Kaen (2003), p.25.

20 Yoshimura and Anderson (1997), p.44.

21 Dore (2000), pp.23-24.

revealed that their BOD really takes major decisions as a result of slimming down the board size. As another fact, several respondents presumed that BOD is the body which takes the decision since it is the place where the matter is finally approved. The in-depth investigations grasped that the major decisions are made at *keiei-iinkai* or *jomu-kai* and the duty of BOD is to ceremonially approve the decision. In many of the cases, now the trend is to have a top level meeting called *keiei-iinkai* replacing the earlier *jomu-kai*. One managing director revealed; 'In addition to board meeting as per the commercial law, we have *keiei-iinkai* which makes all the major decisions for future direction...'

Another director of a company having the traditional governance system explained; 'We did not change our familiar decision making system, because there is no need for such change. The decline in business is not purely due to a governance matter, it is mainly due to economic reasons... As our main market and the owners are in Japan we do not have any outside influence. So what we did was simply advance our familiar *jomu-kai* to *keiei-iinkai* for quick decision making'.

Some participants showed their policy document for establishing the *keiei-iinkai* and the major purpose of such formulation is to accelerate the important decision making and to allow on-the-spot decision making too. Major decision making in small and medium scale companies have not been materially changed. However, they also have shifted to *keiei-iinkai* from *jomu-kai* to enhance decision making. One president of a medium-scale company told; 'We take all our important decisions at our newly formed *keiei-iinkai*. It is faster than our old *jomu-kai*, I feel. At the meeting I try to give hints and guidelines for other senior members for better decisions. Our *keiei-iinkai* final decision is communicated to the BOD meeting as information for other directors and for approval...'

While majority of interviewees revealed that *keiei-iinkai* or *jomu-kai* as the center for major decisions, they did not forget to declare that the CEO dominates the meeting as the leader of the company. However they feel that the level of influence is little bit lower than the past. One vice-president explained; 'we allow our CEO to run the meetings as the head and decide the matters including appointment<sup>22</sup> (BOD & next CEO), calling of meetings, determining goals, performance appraisal...but, now other directors also can contribute after appointing external directors to our board...'

The level of dominating the meetings by the president of small and medium scale

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22 From the stand point of Commercial Law, board of directors should be elected by General Meeting of Shareholders who direct representative directors; usually president or chairman.

companies is comparatively high. But compared to the past they provide guidelines or hints rather than specific orders allowing other members to actively participate.

Respondents of the global companies having traditional governance system confirmed that they make their major decisions at *fuku-shacho-kai* (vice-presidents' meeting) or special management committee which is in a higher position than the previous *jomu-kai*. Conversely the respondents of global companies having either committee system and intermediate system revealed that they make all their major decisions at the BOD meeting. This may be mainly due to the slimming down of their board size for efficient and effective decision making.

### 5.5 Long-term Goals

As one of the important roles, the board as the top level of the entity must formulate the long-term goals and strategies for the implementation by the executive managers and finally monitor the evaluation. Specifically, in the role of evaluating, the board must pay attention to considerable deviations from the set goals. As specified in Table 7, none of the board member of responding firms takes responsibility for inability to attend the set long-term goals. Even though the major decisions are taken by the board or its own committee they do not take any responsibility and resign. At least the CEO as the figure head does not take any responsibility for failure in achieving the set corporate goals. Instead, 46% of the companies just amend the numerical values of the goal before the end of the term and 27% of the companies just amend the numerical values at the end of the term.

The in-depth case studies were able to reveal that the treatments for the

**Table 7**

What does the company do if a long-term goal cannot be attained?	No. of Responded Companies	%
1. The numerical values of the goal are amended	29	46
2. The numerical values aren't amended until the end of a term.	17	27
3. Members of the Board take responsibility, and resigns.	0	0
4. A CEO (president or chairman) takes responsibility, and resigns.	0	0
6. Others	17	27
Total	63	100

Source: Survey Conducted by the Authors in 2004.

unattained goals are not as simple as shown above. In many instances the boards take considerable time to find out the reasons for the failures as a basis for remedial actions. One vice-president of a company having a traditional governance system put in plain words; we call a special board meeting after a *keiei-iinkai* and facilitate to discuss freely the reasons for the failure. We try to find out whether it is due a forecasting error, implementation problem, external impact like market failure, resource allocation problem etc.

Some companies discuss the matter individually outside the BOD meeting as a true fact finding technique and slowly discuss the reasons for the failure and the corrective measures to be taken for immediate implementation. Another managing director of a company having an intermediate system made known; ‘...though we (Japanese people) are slow decision makers, we discuss major deviations each other when and where we (senior directors) meet and consult with the relevant division/s before a formal board meeting (*nemawasi*<sup>23</sup>). Then we deeply discuss the reasons for why the malfunction occurred and the strategies to be adopted as a foundation for quick implementation, instead of just taking responsibility or resigning...’

In global level companies, boards are more serious about such deviations and they take actions beyond the other companies mentioned. Depending on the degree of importance and the contents, they examine the countermeasures against the target achievements. If the failure is within the scope of execution, the actions of responsible executives are reviewed and if necessary training is provided. As disclosed by the respondents, any kind of major deviations are easily detected by their performance appraisal system. One company even tries to publish news release on their homepage if the failure is considerable as such issues are very sensitive for their investors, especially for foreign investors. Most of these companies, they have corporate planning or long-term rolling planning system. If there is any deviation they try to identify the issue as early as possible using their monitoring function and thereafter the reasons and the probable actions are discussed in detail. Finally they direct the issue to the corporate planning committee or section for further improvements to the plan for better results.

In sum disregarding the nature of governance system Japanese boards make possible efforts to grasp any failure through their monitoring function, instead of

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23 Informal prior consultation and negotiation before formal meetings (Otsu and Imanari, 2002), pp. 251-261.

emphasizing on responsibility or resigning. One senior director generalized; 'In Japan we work as a group. Today's companies were brought to this level by both *torishimariyaku* (directors) and *jogyoin* (employees) by working hard together and harmony. If there is a failure every one is responsible, not only the *torishimariyaku*. If the *torishimariyaku* resigns it is another crisis and failure... as they are the corporate elders'.

Mainly the plans are reviewed and depending on the situation, if required they amend the targets. In most of the medium and small scale companies having traditional governance system the issue is firstly discuss within their senior element, *keiei-iinkai* or *jomu-kai* and then have a detail discussions at the BOD meeting with all the head of divisions and bring the news to the employee level when necessary. In addition to above, global companies launch interrelated systems like corporate planning and performance appraisal regarding long-term goals.

## 5.6 Power to Decide the Next CEO

Succession planning for CEO is a vital matter for an entity as far as its continuing future is considered. Therefore each company must have a system to select its next CEO with reasonable care. In relation to Table 8, 56% of the companies' next CEO is decided by the BOD and 19% of the companies the authority is rest with the existing president. Earlier the general acceptance was that the present CEO has more power to decide the successor. This finding shows a substantial shift from the common generalization prevailed some time ago.

The existing CEO has considerable influence to decide the next CEO. Because in practice CEO nominates or appoints the members of the board and this surrounding creates a great obedience toward the CEO by other directors<sup>24</sup>. This enables the present CEO to select the most attractive or closer person for him as the next CEO. A director of a company with a traditional governance system added; '...from the beginning the existing CEO appoints or nominates the next CEO to be, because he is the one who knows more about the next most appropriate person...'

In most of the medium and small scale companies, as usual in the past the next CEO is decided by the present CEO. At present, the participants believe that the selection of the future CEO is a challenging task as far as the competition and the market stagnation are concerned. One senior managing director of a SMC explained; 'Our next

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24 see Vinner, A., (1993).

**Table 8**

<b>Who has more power to decide the next CEO</b>	<b>No. of Responded Companies</b>	<b>%</b>
1. President	12	19
2. Chairman	2	3
3. BOD	35	56
4. Not specially decided.	4	6
5. Others	8	13
Not Response	2	3
Total	63	100

Source: Survey Conducted by the Authors in 2004.

CEO will be decided by our present president as usual. But now it has become a very difficult task to select the best one. Not like in the last 30-40 years ago, the competition is severing within an unstable market...'

Compared to above in global level companies, the situation is more complicated in addition to the domestic issues. In such companies, demands of foreign investors, nature of different legal, cultural and social matters in different markets, technological issues and global competition are some factors influencing the selection of next CEO. One leading company with a traditional CG system mentioned that the appointment is not solely done by the president though he has the power to influence; the board decides the next CEO. Several other leading companies have already set up an advisory committee or appointment committee or personnel committee for deciding the next CEO. A director of a large company having an intermediate system carefully revealed; 'Of course, I think, present CEO has considerable sway. But with the acceleration of globalization, advisory committee has to nominate the best person capable of handling the voice of foreign investors, understanding different cultural, social and legal setups, technological matters, competition and so on. The successor should be able to win all these while winning the other members of the board. When there are non-Japanese in the board the impact is more critical...'

### **5.7 Implementation of Outside Director System**

As given in Table 9, 35% of respondents have already implemented outside directors more than 5 years ago. This 35% includes the outside directors introduced by

**Table 9**

<b>Outside Director System</b>	<b>No. of Responded Companies</b>	<b>%</b>
1. Already implemented more than 5 years ago	22	35
2.. Already implemented during the last 5 years	11	17
3. From now onwards, it will be introduced.	2	3
4. Not interested	6	10
5. Not decided yet	19	30
6. No response	3	5
Total	63	100

Source: Survey Conducted by the Authors in 2004.

the companies as a voluntary measure. Since there was no much research work available on this area, many were unaware of such a development occurred 5 years ago.

However, the rate has been increased remarkably by implementing another 17% of the companies, during the last five years only. Though, only 3% wish to adopt the system now onward, 30% of the companies are uncertain about the adoption. However another 10% specifically decided not to implement such a feature within their traditional CG system.

In several years ago, almost all the outside directors are form affiliate companies as a tradition. Mainly this was due to the common belief that a complete outsider has no comprehensive understating about the company and its industry. Further, the outside director was just to represent either the main bank or parent company. By shifting away from the past situation, as given in Table 10, 55% of the respondents expressed that their outside directors are from non-affiliate companies. Compared to the results of Policy Research Institute of Ministry of Economy and Financial Services in 2003 (see Table 2), this is a remarkable improvement over one year even though the classification is different.

In the detail analysis, it was found that only few companies have included some client organizations, insurance companies and personally contacted companies in this category. Very specifically 6% of respondents who are comparatively small companies declared that they have outside directors from their affiliated companies. On the other hand, lawyers, certified public accountants and scholars are not very popular as outside directors among the respondents.

Table 10

Who are the outside directors? (multiple answers accepted)	No. of Responded Companies	%
1. Directors of other companies (affiliate company)	4	6
2. Directors of other companies (excluding affiliate company)	35	55
3. Lawyer	4	6
4. Certified Public Accountant	2	3
5. Scholar	5	8
6. Others	14	22
Total	64	100

Source: Survey Conducted by the Authors in 2004.

When deeply analyzing the medium and small scale companies with traditional CG system, they prefer a board free of outsiders or in some other cases they prefer outside directors from related or affiliate companies. Their main argument is that the outsiders have no deeper understanding about their company and industry like the insiders who dedicated more than a half of their lives to the company in a very loyal manner. Thus, these companies sometimes simply reject outside directors mainly on the grounds of lack of awareness about the company, they hardly think about any input like innovative information flow from the external environment. This is mainly because of their ability to survive with the lower level of domestic competition. On the other hand, it is implied that they insist on this 'awareness matter', having an understanding that the outsider might take 'business decisions' instead of monitoring as there is no adequate separation between execution and monitoring in such companies. One CEO of a smaller company having a traditional governance system declared; "Recently we introduced few outside directors from our related companies. If they are from unrelated areas, they cannot understand our necessities...(showing the gravity)".

Even though Japanese companies are not entirely new to the outside director system, in many cases they experienced only the outsiders from their group companies. Therefore, in one hand the independent directors are a new system which generates little uncertainty about the way of implementing. In fact they would like to adopt the system once they have a clear view about how a pure outsider can contribute effectively for another company having a little knowledge within this competitive business setup. Another managing director evidenced;



“In this turbulent business environment, every *thorishimariyaku in* (director) is busy in their respective firms. Then, how do they effectively contribute for another completely different company with little awareness about our company? So we have one outside director. He is a son of an ex-director who had extensively contributed to develop the technical side of our company over many years”.

Even if some companies are willing to adopt this system the ‘independence status’ has become a dilemma for them and they are questioning how a director of another company successfully add a value while serving for his respective company. A senior managing director who is eagerly waiting to see the soundness of implementing the outside director system in other companies added; “We are not familiar with this kind of independent external directors. We are just observing the applicability. If it works well in other companies we also implement though it is difficult to find. Sony, ORIX and many others have implemented it. But, for me it is a puzzle that how the COE of ...(name of a global company) contribute in... (name of another global company) effectively with his busy schedule”.

In several cases, the inability of finding independent directors was stressed mainly due to existing *keiretsu* and cross-shareholding systems. On the other hand they are very positive to think that there may be a considerable chance for Japanese companies in the near future for having such system since both *keiretsu* and cross-shareholding systems are in a declining trend; “As you know in Japan we have *keiretsu* groups as well as cross-shareholding networks. Therefore most of the companies are interrelated. It is practically difficult to find so-called independent outside directors. Now with the reforms both the importance and steadiness of *keiretsu* and cross-shareholding have been falling. May be in 5-10 years we will be able to find such directors”.

As an option to find outside directors, other than the popular way of appointing from related companies few companies have already chosen the directors from academic institutions. However, yet the intellectuals haven’t effectively contributed in the boardroom. Most probably this may due to the initial stage of new experiment in the Japanese corporate setup. A director of a company having a traditional system explained about this new source to appoint outside directors; “We have outside directors (from related companies). Now we are seeking for 1 or 2 independent directors form the academic sector. But a friend of mine told me that intellectuals’ role was limited in their board room due to some practical reasons”.

The system is very popular among larger global companies. As revealed through the detailed analysis they expected to absorb the news and information about emerging trends while ensuring independent monitoring over execution. More specifically, in global companies both institutional and individual investors are very much concerned on their investment and the board as the body of accountability has to employ a closer monitoring system which can be easily understandable to those investors in a transparent manner. Furthermore, this kind of appointments is believed to be a basis for going for innovations to meet the global competition in order to gain a competitive advantage over the competitors. In several companies they are looking for a board having majority of outside directors with a chairman who is also an outside director. One director of larger company having Anglo-Saxon committee system positively declared about the prospects of the new system appreciating the reforms introduced through the amendments to the Commercial Law; “We are seeking for new ideas from the external world while ensuring proper monitoring over execution. We hope to utilize every opportunity resulting from the amendments of Commercial Law”.

**5.8 BOD's Impact on Corporate Governance**

This study makes an effort to understand the validity of the preposition ‘the heart of systems of corporate governance is the BOD’ in Japanese context. Based on literature the impact of both BOD and CEO’s mission and role on CG was examined. Interestingly, as shown in Table 11, having the same weight, 46% of the companies declared that both BOD and CEO’s mission and role are very significant.

**Table 11**

BOD's Impact on Corporate Governance	Mission of Board		Mission of CEO	
	No. of Responded Companies	%	No. of Responded Companies	%
1. Most Significant	29	46	29	46
2. More Significant	24	38	22	34
3. Neutral	5	8	6	10
4. Less Significant	0	0	0	0
5. Not Significant at all	0	0	0	0
6. Not Response	5	8	6	10
Total	63	100	63	100

Source: Survey Conducted by the Authors in 2004.

Further, over 80% of companies consider the BOD and CEO impact is at least more significant. Only about 10% of the respondents were neutral about the issue. The respondents who were neutral and not responded were comparatively smaller companies in the sample. The critical studies reiterate the above evidence. A senior managing director of a larger company having a traditional system elucidated; "If we loose the contribution of board members and the CEO, the survival of our CG function is in danger".

Though the following phrase is extracted from a senior managing director of a small scale company, it divulged whatever the size or the existing CG system, the mission and role of BOD is significantly affect the smooth running of the CG. "In total, CG system of our company means our BOD including the president. Apart from that no live CG function here".

The above finding indicates that no matter they have either traditional or Anglo-Saxon committee systems, the BOD and CEO of Japanese companies have an above average influence on their corporate governance systems. This is one of the key recent developments in the Japanese company with regard to CG. Furthermore, there is a good indication that both the monitoring and execution nail clippings are having a principle endeavor to enhance CG in real terms.

### **5.9 Future Actions for a Stronger Board**

This study, having a forward look, attempts to find out the actions to be taken in the near future. As given in Table 12, 60% of the responses assured that the companies are willing to introduce a performance evaluation system for individual directors.

As found under 'evaluation of board performance' this trend is mainly due to the emphasis on efficiency and effectiveness considering the sky-scraping competition. The next most important action to be taken is the review of directors' compensation system as 22% of the respondents declared. As found by the detailed investigations, 1 in 5 companies plan to shift their remuneration policy toward performance based system including board members. One managing director of a large company with a traditional governance system told; "No longer can we continue 'seniority system' within this competitive setup? We take every measure to implement 'performance based system' for rewards even for board members".

All together, the increasing trend of reducing the number of directors in the

**Table 12**

Future actions to be taken by the company for a stronger board (multiple answers accepted) (n=63) (Note: The TSE study emphasized on actions taken)	Present Study		TSE Survey in 2000
	No. of Responded Companies	%	%
1. The reduction of the number of directors	7	11	46.2
2. The review of directors' compensation system	14	22	16.7
3. The evaluation of accomplishing each director's performance	38	60	NA
4. The strengthening of the BOD from other companies	1	2	33.2
5. Others	11	17	27.9

Source: Survey Conducted by the Authors in 2004.

board, introduction of executive directors, and appointment of external directors has been slower since those matters had been considered by most of the companies several years ago. That is why the response is low at the moment for such former actions as specified in Table 12. Proceed from that point forward; nowadays companies are more concern about very specific board reforms such as implementation of performance evaluation and review of remuneration. Most of the global companies having both traditional and Anglo-Saxon committee systems began to think on very specific future actions including; separation and strengthening of monitoring and execution, speed up of the decisions on routine operations and delegation of authority for enhancing their boards.

## 6. Summary and Conclusions

In consequence of globalization and information technology Japanese socio-economic system began to change gradually but continually. As far as the Japanese corporate governance system is concerned, there have been dramatic changes resulted from the revisions to the Commercial Law and Japanese Financial System since 1996. The impact of these alterations has began to make a considerable change inside the Japanese board rooms by introducing some of the new features to their existing governance system such as outside director system, executive officer system, stock options, performance evaluation system, slimming down the boards, disclosures about boards etc. The most significant change is that the shifting of more than 40 larger

companies to the US committee system recently.

This study found the changing nature of Japanese corporate boards using a comprehensive methodology having both questionnaire survey and several critical incidents based on Chell (1993). According to the study there are several CG models across the firms. Therefore the results were discussed under four main test categories namely SMCs, companies having intermediate governance system, large companies having traditional governance system and large companies having Anglo-Saxon committee system.

Leader of the BOD meeting is basically the president as an inherent feature of governance in the Japanese company, especially having a traditional approach to CG. Conversely, the companies which shifted to Anglo-Saxon committee system do not seem to be adhered to such traditional orientation; instead they pursue the rules and norms which followed by the system. Therefore the leader of the BOD meeting is mainly an outside director like in the West.

A large number of the companies have already started to circulate a formal set of proceedings with a notice at least a week before the next board meeting even in several SMCs. However there are still some companies that do not distribute the documents allowing a specific time period before the meeting. Newly restructured companies toward Anglo-Saxon committee system or intermediate system attempt to provide a comprehensive set of materials at least one week before the meeting.

The *keiei-iinkai* or *jomu-kai* is still the center for major decisions in SMCs, however now the degree of dominance by the president is low. Major decisions of global companies having traditional governance system are taken at *fuku-sacho kai* (vice-presidents' meeting) or special management committee which is in a higher position than the previous *jomu-kai*. On the contrary the major decisions of global companies having either committee system or intermediate system are taken at the BOD meeting. Still *ringi* and *nemawashi* are being used by Japanese companies with their advanced versions mainly in the middle level not in the top level. Major decisions are made using contingent approach or consultative and consensus decision making styles as explained by Vroom, Victor, and Yetton (1973).

When attaining a long-term goal is in a doubt, disregarding the nature of governance system, Japanese boards make every possible effort to grasp any failure through their monitoring function, instead of emphasizing on responsibility or resigning.

Mainly the targets are reviewed and if necessary they are amended. In most of the SMCs having traditional governance system the issue is firstly discussed within their *keiei-iinkai* or *jomu-kai* and then detail discussions are held at the BOD meeting with all the head of divisions and bring the news to the employee level when necessary. The global companies launch interrelated systems like corporate planning and performance appraisal regarding long-term goals.

There are many mechanisms to decide the next president in Japanese companies. On average, within the traditional governance setup the existing president has a considerable power to decide the next president. Nevertheless, in all the cases the magnitude of the influence is slightly sinking and majority of companies are assigning the task to the BOD or a committee of the BOD. In particular, in SMCs mostly having traditional governance systems, the selection or the pressure on selection is basically rest with the existing president. However, now, even in such companies the successor is decided based on the ability to cope up with the competitive market conditions. In some global companies having traditional governance system, next president is decided by the BOD though there is a significant pressure from the existing president. Even this also evidences that the level of influence to select the next president solely not in the hands of the existing president; instead the power is being slowly shifted to the board. The leading companies having either intermediate or committee system shifted the power of selecting the next president from president to a board committee; namely the nomination committee to nominate and report it to the BOD meeting.

Generally, about half of the companies have already implemented the outside directors though some of them are not independent in actual terms. Particularly in larger companies having shifted to Anglo-Saxon committee system, there are independent directors similar to their Western counterparts. Disregarding the size and the governance nature, there is a steady increase in introducing the system during the last five years. The SMCs having a traditional CG system are in a doubt though they are willing to implement the system until the pioneers get succeeded.

The finding indicates that no matter the system is traditional or Anglo-Saxon committee, the BOD and president of Japanese companies have an above average influence on their corporate governance systems. This is one of the recently being emerged developments in the Japanese company with regard to CG. Moreover, there is a good indication and tendency that both the monitoring and execution ends are very

keen in enhancing CG further in a true sense.

The increasing trend of slimming down the board, introduction of executive directors, and appointment of external directors has been slower since those matters had been considered by most of the companies few years ago. That is why the response is low at the moment for such former actions as specified above. At present the companies are more concern about very specific board reforms such as implementation of performance evaluation and review of compensation. Nearly every one of the global companies having both traditional and US committee systems have already decided on specific future actions including; separation and strengthening of monitoring and execution, speed up of the decisions on routine operations and delegation of authority for enhancing their boards.

The 'ceremonial nature' of Japanese Corporate Board has been shifting away to some extent and emphasizing more on efficient and effective decision making. In many cases *jomu-kai* has replaced by *keiei-iinkai* with some improved features. The companies shifted either to Anglo-Saxon committee system or to intermediate system have already moved away from the ceremonial board for better top level decisions and monitoring. In contrast, several leading companies having traditional governance system do not allow for any injection to formulate or revise decisions made by *fuku-shacho-kai* or similar meeting having more power than the previous *jomu-kai*. Then the BOD meeting has nothing apart from the ratification of the decisions taken elsewhere. Further, in some incidents companies having traditional approach still conduct the board meeting as a legal formality or a session for progress control & operational decisions and some directors are still engaged in operational decisions of the divisions.

Derived from the above facts, there are numerous patterns of corporate governance have been emerging in Japan as a result of the stimulations granted by the revisions to the Commercial Law. The nature and the role of BODs of companies shifted to Anglo-Saxon committee system and intermediate system have been significantly changed. Now, in those companies there is a considerable segregation between monitoring and execution indicating a tendency to converge towards the Anglo-Saxon model. However, there are some global companies highly resist adopting such new governance system instead they suggest further improvements to their existing system according to the local and global requirements. The SMCs still prefer the traditional model which benefits them over a half a century. Anyhow, SMCs have taken several

steps to improve their traditional system for better governance in their respective companies.

Finally we must emphasize that Japanese traditional system is holding some good aspect for the corporate governance. In Anglo-Saxon countries, the money and the stocks are based on the various kinds of values. So the creation of value directly leads to the maximization of stock prices that forces the top management and boards of directors to pursue the shareholder's value. On the other hand, until recently Japanese companies have believed in the interdependent long-term relationships based on trust and the paternalistic community of fate. That is why the Japanese management system had functioned well before the bubble economy. However, in the process of mega competition the Japanese companies must incorporate non-Japanese management systems including Anglo-Saxon system, in terms of managerial resources and management style. In fact some of the Japanese excellent companies are adopting some part of Anglo-Saxon system and at the same time maintaining the long-term employee-oriented Japanese system which has insured the quality of products and services in the long run<sup>25</sup>.

As a result of deregulation and opening up the market, many business-related laws have been revised and merged. Most important revision is the enactment of new Corporate Law. The existing Commercial Law was enacted in 1899 of *Meiji* era and the Limited Company Law was enacted in 1940. The two main business-related laws will be merged and converged into the new Corporate Law in 2005. This trend does not mean that the Japanese system will completely change from Japanese style to Anglo-Saxon style. The reality is the new Japanese corporate system started to look for the most appropriate style for the Japanese companies in the era of mega-competition.

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