Pay Fight!

Corporate Director Compensation Disputes in Japanese Courts and What to Make of Them

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I. INTRODUCTION

The topic of how, and how much, Japanese corporate executives are paid finds itself at a crossroads between two research questions, one largely descriptive and the other normative. With respect to the former, interest among legal scholars in recent years has focused some attention on the question of why the pay of Japanese corporate executives remains relatively modest in international comparison. Oddly, given the discipline, few of these have actually focused much attention on exploring legal determinants of this trend. Instead attention has been paid to factors such as general corporate

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governance mechanisms[1], cultural aversions to greed[2] or the role of shareholder voting.[3] These focuses make sense to the extent that those factors undoubtedly have some explanatory power, but it has created a body of literature on the topic which doesn't really have much to say about the institution that legal scholars otherwise love to obsess about – litigation in the courts.[4]

With respect to the latter lies the question of whether or not Japan's system of corporate pay is an exemplary model that functions well in its context on the one hand, or if it is a drag on corporate productivity that needs to be urgently reformed to bring the country in line with global market standards on the other. One arguing the case of the first may point to the fact that Japan has for the most part avoided falling prey to the gross disparities between CEO and worker pay that have come to typify practice at large American corporations[5] and, through their contribution to overall income inequality, are imposing costs in a variety of forms on that society. In contrast one arguing the second could claim that traditional pay practices which relied heavily on fixed elements have not adequately incentivized executives which has had negative effects on the ability of major corporations to compete in global markets. The path of current reform strongly suggests that the latter view is dominant in policy circles, but these questions remain.[6]

These two questions – which simply asked "what has caused Japanese corporate executive pay to be the way it is?" and "is this something that needs fixing (and, if so, how)? – provide the impetus for this paper's focus, which is on understanding the role played by the courts in Japan in relation to the pay of corporate executives. This is largely devoted to providing additional insights on the descriptive question, but it also has implications

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1 R. J. JACKSON Jr. / C. J. MILHAUPT, Corporate Governance and Executive Compensation: Evidence from Japan, Columbia Business Law Review 2014, 111.

2 A. R. SALAZAR / J. RAGGIUNTI, Why Does Executive Greed Prevail in the United States and Canada but not Japan? The Pattern of Low CEO Pay and High Worker Welfare in Japanese Corporations, American Journal of Comparative Law 64 (2016) 721.

3 S. MCGINTY / D. GREEN, What Shareholders in Japan Say about Director Pay: Does Article 361 of Japan's Companies Act Matter?, Asian Journal of Comparative Law 13 (2018) 87.

4 Japanese language scholarship has, naturally, paid significantly more attention to case law on the subject than the English language literature, though unlike the former it rarely frames it as a comparative question. For recent Japanese scholarship, see H. HARA［原弘明］, 取締役報酬に関する会社法下の裁判例の概観 ： データベース収録裁判例を素材として [An Overview of Case Law Under the Companies Act Regarding Director's Remuneration: Based on the Judgments Listed in the Databases], 關西大學法學論集 Kansai Daigaku Hōgaku Ronshū 70 (2020) 814.

5 On this see particularly SALAZAR / RAGGIUNTI, *supra* note 2.

6 See discussion in Section II below.

for the normative one as any debate on that question should necessarily be grounded on an understanding of the institutions which have shaped it.

With respect to the general issue of the relationship between executive pay on the one hand and courts on the other in the American literature suing is usually framed as one of the ways in which shareholders exercise discipline over executives.[7] If they do not like it, they can sue, sell their shares or vote against the directors who approved it. "Suing" in this regard is almost always assumed to consist of shareholders using the derivative action to challenge pay decisions based on breaches of director duties in approving it. But is this actually representative of the types of executive pay disputes which courts routinely handle? To get an idea if that is how things work in Japan, the author collected a set of 230 judicial decisions issued between 1953 and 2018 in which the main rule governing corporate director[8] pay, Article 361 of the Companies Act[9] (or its predecessor Article 269 in the Commercial Code[10], hereinafter collectively referred to as the "JSOP rule"[11]), was used in the context of a dispute over the entitlement of a corporate director to their remuneration. The results provide some surprising insights into the litigation of corporate director pay disputes in Japan.

The first insight is that Japanese courts, and particularly the Tōkyō District Court, deal with director compensation disputes quite frequently. This has particularly been the case since the turn of the century, with decisions appearing at a rate of roughly ten per year since 2000. The second insight is that the nature of these litigated disputes differs drastically from the shareholder derivative action narrative developed in the American literature. Article 361 could be loosely described as a type of "Say on Pay" rule, which requires the pay of the board of directors be set either in the articles of incorporation or by a resolution of the shareholders' meeting. This procedural requirement has lent itself to a fairly diverse set of uses in the Courts. Broadly speaking these fall into one of two categories. On the one hand, in keeping with its purpose, the rule has been used by both shareholders and corporations themselves to challenge director entitlements to pay. On the opposite side it has been used with even greater frequency in lawsuits initiated by directors claiming remuneration from corporations. A third insight which follows from the second is that in Japan with respect to director pay litiga-

7 R. S. THOMAS / K. J. MARTIN, Litigating Challenges to Executive Pay: An Exercise in Futility?, Washington University Law Review 79 (2001) 569.

8 The rule only applies to directors (and also *kansa-yaku*, members of the audit board), rather than "executives" more broadly. However, in practice most executives at Japanese corporations are directors and subject to the rule.

9 会社法 [Companies Act], Law No. 86/2005.

10 商法 [Commercial Code], Law No. 48/1899.

11 Japanese Say On Pay (JSOP) rule.

tion in the Courts could more accurately be described as an enforcement mechanism for directors rather than an oversight mechanism for shareholders. The vast majority of the cases which this study uncovered are in fact lawsuits initiated by directors seeking to enforce claims for remuneration against the corporation, with shareholder lawsuits being far less common.

The reason for this lies primarily in the fourth and final insight, which is the important role the courts have played in developing the rule itself. Taking a provision that consisted of a single line which left an enormous number of issues unanswered the courts developed a fairly extensive set of rules governing how it, and by extension how decisions on director pay, operated. In particular as will be elaborated on further below the cumulative effect of these has been to give boards of directors at companies using the predominant "Companies with *kansa-yaku*" system[12], and particularly the representative directors who exercise delegated control over them, a great deal of independent power to set the pay of individual directors. This in turn has put the pay of individual directors, and particularly those who run afoul of representative directors, at some risk which has led many to turn to the courts to try to enforce their claims.

The paper proceeds as follows. Section II briefly reviews the theoretical connection between executive pay and the courts. Section III then provides an overview of some of the institutional forces that previous literature suggests might have an impact on executive pay in Japan. Section IV then presents the cases, reviewing the overall data on litigation they provide and providing a detailed narrative about how the case law has evolved over time, what issues have arisen and how the courts have dealt with them. Section V then discusses the implications of these findings and conclusions follow.

II. EXECUTIVE PAY AND COURTS

How do we define the role of the courts with respect to executive pay? This question entails both a descriptive and a normative element and we may begin by first addressing the former. The dominant view, or at least the only one which underlies most research related to this question, is that the courts serve as a forum for shareholders to use derivative actions to sue officers in relation to decisions on executive pay contracts that were reached in violation of their corporate law duties.[13] This literature comes from the United States, where it has been developed in the context of the various rules and

12 The Companies Act gives corporations three alternative forms they may adopt which feature different board structures following reforms in 2002 and 2015, see *infra* note 40. The traditional Companies with *kansa-yaku* system remains dominant and all the cases in this study stem from companies incorporated as such.

procedures available in that country, particularly in Delaware. The debate has also been influenced by the context of the explosion of executive pay levels there over the past forty years and the rise of the view that the main goal of executive pay contracts is to align the interests of executives with the corporation as the most efficient means of reducing shareholder agency costs.[14] Scholarly debate has thus often been reduced to a question of whether pay packages adequately accomplish this goal, or if defects in the pay setting process allow executives to structure their pay in overly generous ways that do little to provide proper incentives.[15] Regardless of where one falls within that spectrum, the issue is almost inevitably framed as one in which shareholders face the adverse consequences of poor decisions and thus unsurprisingly discussion of the role of courts have focused on their use by shareholders as a mechanism to monitor or challenge executive pay. Since derivative actions alleging breaches of director duties is what American law gives to American shareholders, that literature has further focused its attention on that specific mechanism for redressing the problem.

This focus is understandable, but even in the American context only gives us a partial picture of how the courts are used, leaving questions like whether shareholders use means other than derivative actions to challenge pay, or to what extent other stakeholders use the courts unanswered. As the author has noted in a separate paper looking at the issue in the Canadian context[16] the focus on derivative actions also does not provide a useful framework outside the United States where that option might be either unavailable or seldom used in a given jurisdiction, even where executive pay disputes might be frequently litigated. To understand the role of the courts, we first need to understand a number of factual situations. Who brings claims to the courts? What types of claims do they bring? How do courts respond? Have trends evolved over time?

In addition to these descriptive issues we must also consider some evaluative and normative questions which are largely lacking from the existing

13 See for example THOMAS / MARTIN *supra* note 7; R. S. THOMAS / H. WELLS, Executive Compensation in the Courts: Board Capture, Optimal Contracting and Officer's Fiduciary Duties, Minnesota Law Review 95 (2011) 846; L. M. FAIRFAX, Sue on Pay: Say on Pay's Impact on Director's Fiduciary Duties, Arizona Law Review 55 (2013) 1.

14 This stems from M. C. JENSEN / W. H. MECKLING, Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure, Journal of Financial Economics 3 (1976) 305.

15 The most prominent work advocating this view is L. BEBCHUK / J. FRIED, Pay Without Performance: The Unfilled Promise of Executive Compensation (2004).

16 S. MCGINTY, The Courts and Executive Compensation in Canada, Law and Development Review 14/2 (2021) 753.

English language literature[17], particularly that focused on executive pay in Japan.[18] Implicit in most of this and indeed in much of the debate on legal reform on the topic has been the notion that corporate Japan needs to adjust its executive pay system to better accommodate international market standards.[19] The main focus of the corporate governance related commentariat has thus been on the benefits of shifting away from stable pay arrangements and towards increased reliance on incentive based systems as seen in the United States and other countries. This is reflected in a variety of areas notably including the content of reforms to the Companies Act[20], the introduction of Japan's first Corporate Governance Code[21], the Financial Services Agency's Guidelines for Investor and Company Engagement[22] and the voting policies of proxy advisory services like Institutional Shareholder Services (ISS)[23] to name a few.

This focus is, in a word, odd when viewed from a global perspective in 2021. As noted above in the United States and other countries the systems of

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17 A small but growing Japanese language literature on the regulation of director pay has developed in recent years, most of which is tied to policy discussions on Companies Act reform and how the pay setting practice is changing in response to international market demands. See for example HARA, *supra* note 4; M. KUROKI [黒木松男], 取締役報酬規制の動向と課題 ―令和元年会社法改正を契機として [The Trend and Subject Relating to Director's Remuneration Regulation with Corporate Law Reform of 2019], 創価ロージャーナル Soka Law Journal 14 (2021) 83.

18 A notable exception is SALAZAR / RAGGIUNTI, *supra* note 2.

19 This is not limited to compensation alone but to corporate governance generally. Bruce ARONSON for example began a recent paper by noting the commonly held observation that "From a foreigner's perspective, Japan may appear to be stuck in an unresponsive corporate governance system that favors employees over shareholders and has poor monitoring of management." B. ARONSON, Japanese Corporate Governance Reform: A Comparative Perspective, Hastings Business Law Journal 11 (2015) 85.

20 The most recent amendment, passed in 2019 and came into force on 1 March 2021, among other things has clarified the process of approving equity-based compensation under Article 361 of the Companies Act.

21 Principle 4.2 of the Code explicitly encourages remuneration systems for management to include incentives. Tōkyō Stock Exchange, *Japan's Corporate Governance Code*, available at *https://www.jpx.co.jp/english/news/1020/b5b4pj000000jvxr-att/20180602_en.pdf* (last accessed 19 May 2021).

22 3.5 of which asks companies to consider if their remuneration systems act as a healthy incentive and if an independent committee was involved in their formation. FINANCIAL SERVICES AGENCY, Guidelines for Investor and Company Engagement, available at *https://www.fsa.go.jp/en/news/2018/follow-up/20180601/01.pdf* (last accessed 19 May 2021).

23 ISS Japan Proxy Voting Guidelines Benchmark Policy Recommendations, 2020 is formulated with a clear preference for raises in compensation ceilings to accommodate incentive-based systems and against raises unconnected to incentives.

incentive-based compensation which Japan is now seeking to emulate have played a significant role in causing the explosive growth in executive pay levels over recent decades. These have reached such a degree that they are having macro effects on the increasing overall levels of income inequality generally[24] and are contributing to the deleterious social, economic and political consequences attendant thereon. The focus of much of the debate there in recent years has thus become notably more critical of incentive based executive pay systems[25] and much (though certainly not all) of the literature, including that on the role of the courts[26], could loosely be described as trying to answer the broad question of "how do we control this problem?"

This creates an irony in the path of legal reform – Japan is trying to copy elements of (largely) American executive pay practice at the same time that Japan's own pay system is looking attractive as a point of comparison for precisely the reason that it is not dominated by the effects of those very same features. To a certain extent it fits with what BAUM refers to as "legal fashion"[27] to describe transplants that seem intended to satisfy external expectations on the path of reform in a given jurisdiction rather than to solve functional problems which actually exist within it. The parallels with the focus on independent directors as a subject of Japanese corporate law reform long after their usefulness in the United States and elsewhere have come to be questioned are also hard to miss.

For the purposes of this paper however these normative issues – in other words an evaluation of whether the current course of corporate governance reform with respect to executive pay is heading in the right or wrong direction – need not be resolved directly, but they are important to note since they relate to the value and importance of studying the court's role thus far. Are we studying an institution that has helped create a more equitable model for pay practices that benefits Japanese society as a whole by preventing harmful corporate externalities associated with extreme inequality? Or are we studying one which has helped saddle Japan with corporate pay practices that do not adequately incentivize executives, harming the competitive-

24 J. W. KIM / B. KOGUT / J. YANG, Executive Compensation, Fat Cats and Best Athletes, American Sociological Review 80 (2015) 299.

25 B. C. TINGLE, How Good are Our "Best Practices" When it Comes to Executive Compensation? A Review of Forty Years of Skyrocketing Pay, Regulation and the Forces of Good Governance, Saskatchewan Law Review 80 (2017) 387.

26 See for example L. M. FAIRFAX, Sue on Pay: Say on Pay's Impact on Director's Fiduciary Duties, Arizona Law Review 55 (2013) 1.

27 H. BAUM, Comparison of Law, Legal Transplants and International "Legal Fashion" in German and Japanese Corporate Law, Max Planck Private Law Research Paper No. 20/19 (2019).

ness and productivity of Japanese corporations and thereby lowering the welfare of that same society?

Answers to the descriptive questions – put simply, what have the courts done? – will not answer these normative ones, but are nonetheless key to informing an inquiry into them. In order to provide context within which the role of the courts must be considered, the following section reviews some of the previous literature on the institutional setting affecting pay in Japan.

III. Japanese Corporate Governance and Director Pay

This section draws on previous literature on both Japanese corporate governance and executive compensation in order to provide a framework for understanding the potential role of the courts and to give the discussion on the cases discussed in section IV some context. The section particularly focuses on five interconnected areas: the employee-centered system of corporate governance, the role of norms, the market for executive talent, the structure of the board of directors, and the role of shareholder voting.

1. Employees' Role in Corporate Governance

While the overall system of corporate governance in the United States is often described as having evolved over the late 20th century from a managerial model to one based on shareholder primacy[28], Japan's has followed a quite different path. The post-war system is generally characterized as having consisted of a series of institutions – the main bank system, *keiretsu* groups with considerable cross-shareholdings among members, and the lifetime employment system – which largely rendered the role of shareholders irrelevant.[29] The role of employees is often described as central,[30] backed up by a reciprocal bargain in which the company implicitly guarantees long term employment in exchange for loyalty and devotion to the company.[31] This displays itself in the decision making process by manage-

28 See L. A. STOUT, On the Rise of Shareholder Primacy, Signs of its Fall, and a Return of Managerialism (in the Closet), Seattle University Law Review 36 (2013) 1169.

29 R. K. MORCK / M. NAKAMURA, A Frog in a Well Knows Nothing of the Ocean: A History of Corporate Ownership in Japan, in: Morck (ed.), A History of Corporate Governance Around the World (2007) 367.

30 G. JACKSON, Employment Adjustment and Distributional Conflict in Japanese Firms, in: Aoki et al. (eds.), Corporate Governance in Japan: Institutional Change and Organizational Diversity (2007) 282.

31 Č. PEJOVIĆ, Changes in Long Term Employment and Their Impact on the Japanese Economic Model: Challenges and Dilemmas, ZJapanR / J.Japan.L. 37 (2014) 51.

ment, which is more likely to prioritize protecting employees over attending to shareholder interests such as paying dividends.[32] It is also suggested that internal monitoring of corporate management by employees is primary and that they, rather than shareholders, are the main principals in the corporate relationship.[33] This has obvious implications for the role of litigation since employees have no formal legal mechanisms by which to police executive compensation. It also needs to be noted, however, that owing to a variety of factors most aspects of this system have been eroded since the 1990s to the extent that blanket descriptions of Japanese corporate governance as employee-centered may no longer be fully accurate, particularly at large companies which have actively sought to move away from it.

2. *The Role of Norms*

One of the most often cited theories used to explain the difference in Japanese and American executive pay is that social norms prevalent in Japan serve as a general restraint.[34] The specific content of such norms is never fully explored in the literature, but it is generally conceived that an "outrage factor" will be triggered at a much lower level of pay than in the United States, reflective of the differing role of employees, banks and related firms in corporate governance in general. This is often closely tied to the above-mentioned centrality of employees as the most privileged stakeholder in Japanese corporate governance. Employees as a stakeholder group may be more sensitive to relative pay discrepancies than shareholders, and the directors of Japanese companies, who are mostly employees themselves, may have internalized these norms and be more susceptible to informal means of enforcement than outsiders and thus self-police their own demands for pay. Given the decline of many institutions associated with the employee-centered model, the persistence of these norms may themselves gain greater importance as a check on pay rather than simply being part of the background furniture.

3. *The Market for Executive Talent*

At the heart of most executive pay disputes in the United States are contracts between outside CEOs being brought in to a company, such as in the famous

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32 G. OLCOTT, Whose Company is it? Changing CEO Ideology in Japan, in: Whittaker / Deakin (eds.), Corporate Governance and Managerial Reform in Japan (2009) 195.

33 Z. SHISHIDO, The Hidden Problems of Japanese Corporate Governance and Their Solutions, Delaware Journal of Corporate Law 25 (2000) 189, 189-90.

34 See especially SALAZAR / RAGGIUNTI, *supra* note 2; JACKSON / MILHAUPT *supra* note 1.

series of Delaware cases involving Disney's contract with its short-termed CEO Michael OVITZ.[35] Such contracts arise out of the existence of a liquid market for executives that exists in the United States in which top officers often work for multiple companies over the course of their careers. The existence of this market is also key to pay levels, since industry comparisons play an important role in establishing pay policies. In Japan the market for executives is much less fluid owing to the existence of the lifetime employment system. The presidents of most Japanese companies are generally insiders promoted from within[36], often after being selected and groomed by the current president for the position. They generally hold the position for a single term[37] and a majority move on to become chairman of the board once their term retires, assuming no scandals have marred their tenure.

The terms of their pay are not the result of contractual negotiation as they are in the United States, and as shall be discussed in section IV below, there can a great deal of difference in how pay is set between rank and file directors and representative directors who may have delegated power to set pay policies. Owing to the existence of the lifetime employment system, there is very little external market for executive talent in Japan in general since having left one's company is generally a sign of having done something wrong. While there are some exceptions to this rule, particularly with respect to foreign executives whose hiring process more closely resembles that in the United States[38] these remain a relatively small minority of the total.

4. *The Board of Directors*

In the United States the role of the board of directors is generally a monitoring rather than a managerial one and its structure and composition reflects this. Boards are primarily composed of independent directors and are organized into committees that reflect the intended monitoring role of the board. In Japan on the other hand, the board of directors has traditionally played a managerial role, which was reflected in the wording of the Com-

35 See a comparative discussion of the Disney litigation in F. A. GEVURTZ, Disney in a Comparative Light, American Journal of Comparative Law 55 (2007) 453.

36 See OLCOTT, *supra* note 32; R. DORE, Insider Management and Board Reform: For Whose Benefit?, in: Aoki / Jackson / Miyajima (eds.), Corporate Governance in Japan: Institutional Change and Organizational Diversity (2007) 370-395.

37 S. AHN / U. BHATTACHARYA / T. JUNG / G. NAM, Do Japanese CEOs Matter?, Pacific Basin Finance Journal 17 (2009) 628.

38 This is examined in JACKSON / MILHAUPT, *supra* note 1. The well-known case of former Nissan Chairman Carlos Ghosn, who before fleeing the country while awaiting trial for criminal charges related to his pay had for many years been among Japan's highest paid executives, is a prominent example of this.

mercial Code and later Companies Act provisions defining its function.[39] Rather than being stocked by independent outsiders, the vast majority of directors are internally promoted employees. While reforms since the turn of the century have sought to emulate aspects of the American system – such as through the introduction of alternative board structures – these reforms have been optional rather than mandatory and a majority of companies have declined to adopt them.[40]

As Ronald DORE notes[41] one effect of this is that the purportedly arms-length negotiations between boards and outside CEOs which result in pay agreements in the United States are not typical in Japan. Rather, candidates are weeded out through a long internal process as they proceed up the promotion ladder and their compensation is largely based on existing precedent. Another important point to mention is that the compensation of members of the board of directors itself, largely ignored in the American literature since most are part timers whose pay as directors is relatively insignificant, is of much greater significance in Japan. Throughout the post-war period a position on the board was the highest rung on the promotion ladder for employees at most companies, with some becoming quite large as a result.[42] Presidents are generally groomed while serving on the board and, once they complete their service in that position a majority take on the position of chairman of the board.[43] In terms of compensation, a position on the board seems to be the highest compensated in the corporate hierarchy at most Japanese companies. This is important because the JSOP rule requires shareholder approval of compensation paid to directors *as directors* but not for compensation paid for their duties in a non-director role, but even for those with dual positions such as presidents their pay is often approved by the shareholders. When Kohji TANABE, the representative director and

39 Art. 362(2) Companies Act.

40 The 2002 reform which introduced the first of these, the Company with Committees system, is discussed in R. J. GILSON / C. J. MILHAUPT, Choice as Regulatory Reform: The Case of Japanese Corporate Governance, American Journal of Comparative Law 53 (2005) 343. An important point to note is that adopting the Company with Committees system allows companies to opt out of Article 361 of the Companies Act. A second reform in 2015 introduced a second alternative, the Company with Audit and Supervisory Committee, which is a bit of a crossover between the other two. Director compensation at those is subject to Article 361. The majority of companies use the "traditional" structure rather than those introduced in either of these reforms, though companies have begun using the 2015 option at noticeably higher rates than the 2002 one.

41 DORE, *supra* note 36, at 390–391.

42 In recent years however, the size of boards at large companies has decreased significantly.

43 AHN et al., *supra* note 37.

president of auto-parts maker U-shin, became one of the highest paid executives in Japan in 2014 for example his pay, consisting of 775 million yen in base pay (approx. 6 million Euro) and a 630 million yen bonus (approx. 4,9 million Euro), was entirely his pay *as a director* and followed the approval process as such.[44]

5. *The need for shareholder voting*

The shareholder voting which the JSOP rule requires is itself part of the institutional mix related to pay. A previous paper co-written by the author[45] found that while voting seems to have had little impact through most of the post-war period, largely owing to the above noted features of Japanese corporate governance which tended to sideline shareholders, changes in recent years have given it some additional relevance. In particular the rise in foreign shareholders in Japan with differing views on pay have led to notable differences in vote outcomes associated with factors including the share of foreign ownership in a company and also the type of compensation being voted on. Thus, it could be viewed as a feedback mechanism which is contributing to, if not necessarily driving, the shifting views on pay noted earlier.

6. *Summary*

It is important to note that the above factors describe a quite fluid set of institutions that are constantly evolving, rather than static features of Japanese corporate governance. As noted many of these have in fact come under considerable strain since the 1990s as large Japanese corporations have increasingly been exposed to international markets and actors that have differing sets of expectations. The above review does however suggest a few points about how the potential role of the courts as it has developed over the post-war period might be understood in Japan.

The first is that the employee-centered system of corporate governance created its own set of normative views on what and how corporate executives should be paid. Concerns over structuring pay to minimize shareholder agency costs were not a factor driving these norms, though in more recent years such views have gained some salience. The second is that shareholder interests were generally less well protected by the corporate governance system, an issue that has led many reform efforts in recent decades which have sought to ameliorate it. This suggests the possibility that share-

44 Based on U-Shin's Securities Reports for 2014 and its 2014 Shareholders Meeting Report. This pay resulted in a derivative lawsuit by shareholders which is discussed in section IV below.

45 MCGINTY / GREEN, *supra* note 3.

holders may have had reason to make recourse to the courts regarding pay decisions which may not have reflected their interests. Third, is the fact that the types of executive pay contracts that seem to drive much litigation in the United States for the most part did not exist in Japan. To be certain, Japanese executives of course have contractual relations with their employers, but these were part of a lifetime employment system, with the executives of large companies generally being employees for whom nomination to the board was another step in their career ladder. Their pay was not subject to negotiation with compensation committees but rather set by internal pay rules set by the board.

For the most part the American derivative action-based literature does not provide us with much means of assessing what kinds of disputes might arise from such a system, how the courts might be used or how the role of the court may have changed over time. To figure that out, and also to assess the legal avenues available to the various corporate stakeholders that might make use of the courts, the next section turns to a discussion of the case law which, perhaps unsurprisingly, demonstrates a radically different situation in Japan.

IV. The Case Law on Director Pay

1. *Overview*

In order to get a better understanding of the litigation of executive pay disputes before Japanese courts this study put together a set of judicial decisions involving the JSOP rule (either Article 269 of the Commercial Code or its successor provision Article 361 of the Companies Act after 2005), the main rule governing the pay of directors. These were collected from the Westlaw Japan database using their note up function for each provision, with cases falling between 1953 (the earliest reported) and 2018 (the most recent available at the time the cases were collected). The substance of the cases on each list produced were then checked, with the criteria for inclusion being that the case must have involved a substantive dispute with respect to a director's entitlement to either all or part of their compensation. Generally, these fall under two broad categories. First are cases "challenging compensation" which mostly involve shareholders using a variety of means to challenge resolutions approving pay, or corporate claims against former directors seeking repayment of compensation improperly paid (such as that which had not been approved by the shareholders). The second are cases "defending compensation" which generally involve directors suing the corporation for compensation they were not paid. Excluded were cases which did not involve disputes over pay among corporate constituencies (such as tax cases in which the government was a party) or in which the provisions were only mentioned in passing but were not central to the dispute.

2. *The JSOP Rule*

Here we can say a little bit about the nature of the JSOP rule and what it applies to, which is necessary to make the subsequent discussion of its role in litigation make sense.[46] The rule was introduced in the Commercial Code in 1898 and simply requires that the compensation of directors must be either set by the articles of incorporation or by a resolution of the shareholders' meeting. While Corporate law reforms in Japan have in recent years introduced two alternative corporate forms for the general business corporation to take[47] the traditional corporate form in Japan, which still dominates today, consists of a board of directors and a board of *kansa-yaku* (tasked with some oversight of the board of directors) and all the cases involve such companies. Throughout most of the period examined the JSOP rule on the books remained the same as it had been since 1898, but since 2002 it has been amended three times. The 2002 amendment specifically listed the types of remuneration which had to be fixed by a shareholders' resolution and introduced a requirement that directors explain at the shareholders' meeting any remuneration that is not in a fixed amount or not in a monetary form. The second amendment in 2015 accompanied the introduction of the Company with Audit and Supervisory Committee system which companies could adopt, one of the two mentioned above, and provided special rules governing them. The most recent amendment, which came into effect in March of 2021, specifies that stocks and options given to directors must also be approved by shareholders' resolution. It also provides that companies must disclose their policies for deciding the compensation of each individual director, something not previously required.

For the purpose of this paper the main point of interest of these legislative reforms is what they reveal about how the Courts have developed the JSOP rule over the years, which we cover in the following sections. For the most part the amendments have not altered the fundamentals of the original rule. Rather they consist largely of either clarifying points that had already been addressed in the case law (particularly the 2002 reform) or, as we shall see, addressing shortcomings with the Court's approach (particularly with respect to the 2021 reform's focus on disclosing policies for determining the remuneration of individual directors).

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46 For a more detailed discussion of the rule, see MCGINTY / GREEN, *supra* note 3 at 95–101.

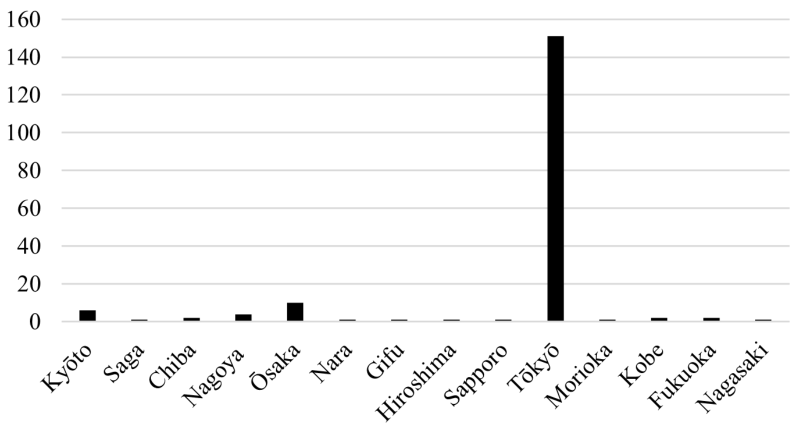
47 The Companies with Committees system (2002) and the Companies with Audit and Supervisory Committee system (2015).

3. *Some Descriptive Data*

Overall the search turned up a total of 230 decisions. Of these, 184 were District Court (trial court) decisions, 31 were High Court (appellate court) decisions and 15 were Supreme Court of Japan decisions. In this section we can review some of the aggregate data these produced to get a general idea of where and when these cases came from and how they were dealt with.

To begin with we can consider the question of "where" the cases originated. As Chart 1 indicates, the overwhelming majority of District Court decisions were handled by the Tōkyō District Court, which alone accounted for slightly over eighty percent of cases. This number however conceals a temporal division. In the decades up until 1980 the Ōsaka District Court (and High Court) actually dealt with slightly more cases than the Tōkyō Courts and produced some of the most notable early decisions, and courts in other regions also contributed a significant number. From 1980 onwards, the Tōkyō Courts began to dominate, and in recent years this domination has become complete. Of the 86 cases since 2010, only 2 of them came from outside of Tōkyō (one in Chiba and the other in Saga).

Chart 1: District Court Decisions by Court



This brings us to a second question which is how the number of decisions has evolved over time. As Chart 2 below illustrates at least in terms of case volume there have been three distinct phases. In the 1950s and 1960s reported decisions were generally few and far between. From the 1970s to the 1990s the total number of cases was higher but remained relatively constant with an average of about two per year. Then from 2000 onwards the number of cases exploded, with 77 coming in the 2000-2009 decade and 86 in the 2010–2018 period. The number of cases in 2018 alone (15) is almost equal to the number of cases for the entire decade of the 1970s (16). This increase in the number of cases it should be noted coincides with a broader, though perhaps temporary, increase in litigation rates in Japan in general in recent years[48] and does not necessarily indicate that director compensation per se has become more contentious over that time, though this may have also been a factor. These numbers also mask significant changes over time in the substance of the disputes ending up in court, which will be elaborated upon in section IV below.

Chart 2: Decisions at all Court Levels by Decade

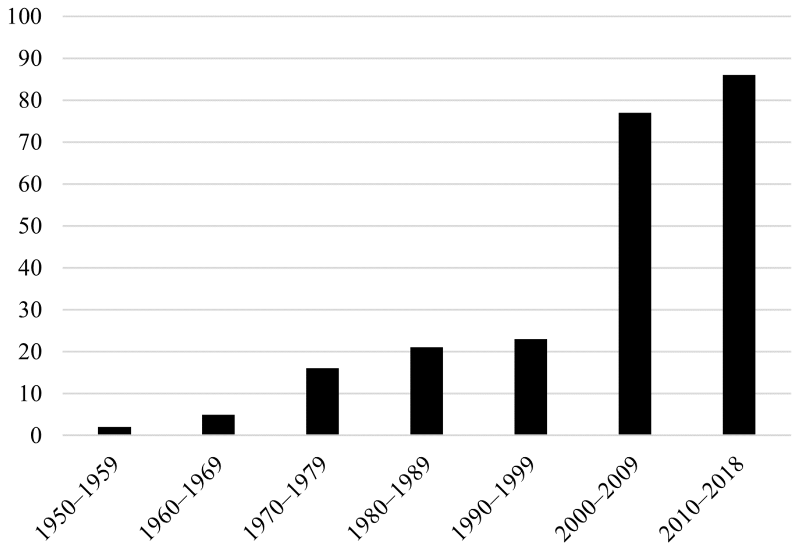


Chart 3 below breaks the District Court decisions down by plaintiff type. Plaintiffs classified as a "Director" in the below chart it should be noted also include a small number of *kansa-yaku* whose pay is subject to substantively the same rule[49], and in a number of cases representatives of the estate of deceased directors. As the Chart indicates, directors are the plaintiffs in the vast majority of cases, while shareholders and corporations are far in

48 Much of the increase in litigation rate between 2006 and 2010, when rates spiked, has been attributed to a rise in consumer loan related litigation which followed a Supreme Court decision on interest rates. See generally G. F. COLOMBO / H. SHIMIZU, Litigation or Litigiousness? Explaining Japan's "Litigation Bubble" (2006-2010), Oxford University Comparative Law Forum 4 (2016) at *ouclf.law.ox.ac.uk.*

49 Contained in Article 387 of the Companies Act.

the minority. This is an interesting and unexpected finding given that the purpose of the JSOP rule is to limit the ability of directors to set their own pay. This will be discussed in further detail in section IV below, but the short answer to the question of why so many director-plaintiff cases appear is that the JSOP rule is often raised as a defence by corporations in director lawsuits seeking pay, which are fairly common. Of the two cases classified as "other" one involved a trustee in bankruptcy and the other was an odd case that pitted a husband against a wife following a divorce.[50]

Chart 3: District Court Cases by Plaintiff Type

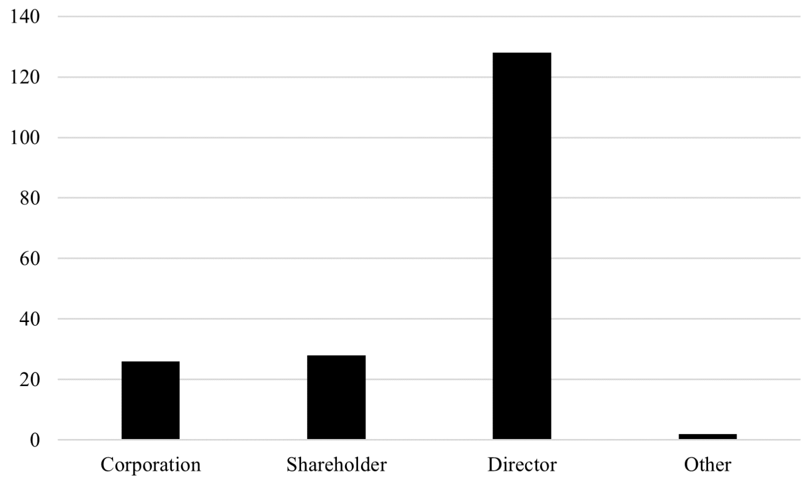


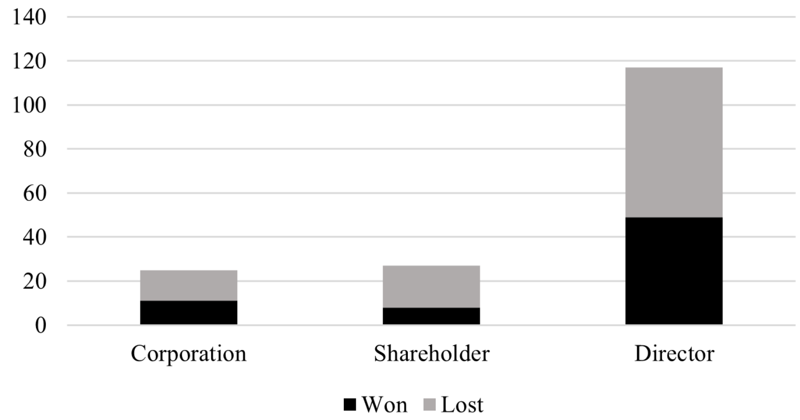
Chart 4 provides a breakdown of how the District Courts responded to the claims brought by each type of the three main types of plaintiff. As it indicates the courts were generally unkind to all kinds of plaintiffs, rejecting a majority of the claims for each. Shareholders had a noticeably more difficult time, with just a 32% success rate compared to corporations (46%) and directors (42%).[51] These numbers also conceal a great deal of variety in the

50 In that case the company was a limited company (*yūgen kaisha*) at the time of the facts of the case, to which the JSOP rule did not apply. Tōkyō District Court, 5 March 2007, Westlaw Japan 2007WLJPCA03058004.

51 The data in Chart 4 include cases which ended in mixed results (i.e. partial success for the plaintiff) which are recorded as a "win" for the plaintiff. There were only a small number of cases (one for corporate plaintiffs and one for shareholder plaintiffs) which ended in such result. In cases where multiple claims or counterclaims were being advanced by the parties, some of which were unrelated to director compensation, the data only accounts for success or failure on the part of the claim related to the compensation dispute.

types of claims advanced by each type of plaintiff, which will be discussed more in the following section.

Chart 4: Success Rate by Plaintiff Type



4. Litigating Director Pay

Having laid out some general data about where and when claims have been brought (mostly since 2000, mostly to the Tōkyō District Court), who brought them (mostly directors but also some by shareholders and corporations) and how they did (plaintiffs lost the majority, especially shareholders) in this section we turn to a more detailed analysis of the substance of the cases in order to give those numbers some actual meaning. Before describing the development of the case law, it is important to draw a quick map of the starting point at the beginning of the development of court decisions from 1953 onwards and how Article 269 of the Commercial Code regulated director pay. At the time it simply stated:

> "If the amount of remuneration to be received by the directors has not been fixed by the Articles of Incorporation, it shall be fixed by the resolution of a general meeting of shareholders."

Article 280 of the Code applied the same terms to the pay of *kansa-yaku* but otherwise the Code was silent on the issue of compensation. This left quite a few things unclear. To begin with the very assumption underlying the provision – that directors were to be compensated – created friction with Article 254 of the Code which stated that "the relations between the company and the directors shall be governed by the provisions relating to mandates." This was a reference to the Civil Code provisions on mandates, Article 648 of which specified that mandatories were, in the absence of agreements to the contrary, not to receive compensation. Furthermore it seemed to put directors in an awkward conflict of interest position since it required them to exercise their authority as directors to put items on the agenda of the shareholders' meeting in which they evidently had a self-interest (their own pay) and the existing provision on such transactions, Article 265, did not seem to adequately address this (since it required board approval for such transactions by individual directors, but compensation matters affected the whole board which would in effect have to ask itself for approval).

Moreover, the provision was completely silent with regard to some pressing practical questions – how much detail of the compensation did shareholders need to be apprised of? How often did they need to approve of it? Did it apply to all forms of compensation or only base pay? What obligations did the board come under once the shareholders had passed a resolution on director pay? How did a resolution affect a director's contractual rights to pay? In looking at how the courts resolved these questions we begin by looking at the case law on suits initiated by shareholders and corporations, which were fairly well represented in the early cases.[52]

5. *Challenging Director Pay – Shareholder and Corporate Suits*

a) *Overview*

By placing director pay in the hands of the shareholders' meeting, the JSOP rule has had the effect of tying shareholder litigation against director pay closely to the rules governing shareholders meetings themselves. This has meant that shareholders have been able to avail themselves of the same remedies used to attack director pay as are available with regard to any resolution of the shareholders' meeting. The Commercial Code provided (and the Companies Act today continues to provide) two general avenues to pursue this – a claim seeking a declaration of the invalidity or non-existence of a resolution[53], or a claim seeking the revocation of a resolution.[54] The former of these may be used to attack the substance of the resolution – in effect advancing arguments that the resolution did not comply with the substantive requirements of the JSOP rule, while the latter allows

52 During the period from 1953 to 1989 23 out of 44 decisions (52%) were in cases brought by shareholders.

53 Originally in Article 252 of the Commercial Code, now in Article 830 of the Companies Act.

54 Originally contained in Article 247 of the Commercial Code, now found in Article 831 of the Companies Act.

them to be challenged based on procedural defects, such as a failure to comply with procedural rules governing the shareholders' meeting at which they were approved. Importantly both of these have a very serious effect for directors – the retroactive nullification of the resolution which approved their pay in the first place. Of the 27 cases in which shareholders were the plaintiffs the majority, 17 in total, are either claims seeking a declaration of invalidity or non-existence of a resolution (8 cases) or the revocation of a resolution (9 cases).

b) Early Shareholder Cases: Challenging the Substance of Resolutions

The very first case in our study was an Ōsaka District Court decision from 1953[55] which involved a shareholder asking the court for a declaration of invalidity with respect to a resolution that had approved a raise in the base pay of the corporation's directors and *kansa-yaku*. The main business of the corporation was running the Shin-Ōsaka Hotel, which at the time the resolution had been passed was being fully occupied by American military personnel. The underlying cause of the dispute was the plaintiff shareholder's belief that since the hotel was occupied by the military (meaning there was very little business for the board to actually do) there was no business basis for the raise. Two main lines of legal argument were brought against the raise. The first focused on the fact that the resolution did not specify how much was to be paid to each director individually, but rather approved a global amount for everyone and left decisions on how it was to be distributed to the discretion of the board. This delegation to the board seemed to create a logical impossibility when considered in conjunction with Article 260-2 of the Commercial Code, which stated that no person with a particular interest in a board resolution could vote on it. Since all members of the board would obviously have an interest in a resolution approving their own pay, this seemed to preclude the entire board from exercising the discretion the resolution in question had granted to it. The second focused on the fact that the resolution in question put not only directors pay but also that of *kansa-yaku* at the discretion of the board, which seemed to undermine the general structure of the corporation itself. The function of the *kansa-yaku* was to inspect the records kept by the board of directors and to issue opinions to shareholders on the documents the board submitted to a shareholders' meeting. This would be seriously undermined, however, if their own pay was subject to the discretion of the very directors they were intended to oversee.

The court began its reasoning by describing the purpose of Article 269, which is to prevent directors from arbitrarily abusing their position with

55 Ōsaka District Court, 29 June 1953, 下民 Kamin 4, 945.

respect to pay at the expense of the corporation – a statement that would be routinely repeated by courts in years to come. It held that a resolution such as this one which approved a global amount and then subjected decisions on how it was to be distributed to the discretion of the board was sufficient to achieve this purpose. Ensuring the independence of *kansa-yaku* was not part of that purpose and thus such concerns were not relevant. Since the purpose of Article 260-2 had a similar purpose to Article 269 of the Commercial Code – protecting the corporation from self-interested behavior by directors – it somewhat dubiously held that it did not apply to resolutions such as this one. The plaintiff's claims were dismissed.

While the decisions of District and High Courts have no binding precedential effect in Japan, several aspects of the decision would nonetheless shape executive compensation claims and corporate governance in general for years to come. To begin with it established that resolutions approving aggregate rather than individual director pay complied with Article 269, a practice that continues to this day. It also validated the practice of subjecting the pay of *kansa-yaku* to the discretion of the board of directors, which is one of the factors which severely undermined the efficacy of the *kansa-yaku* as an oversight organ within the corporation. Finally, it also established the authority of the board of directors to exercise discretion with regard to how to distribute its own pay, another practice which continues to this day.

Shareholders in the late 1950s and 1960s brought subsequent claims which tested the issues raised in the 1953 judgment. The issue of subjecting *kansa-yaku* pay to the discretion of the board was challenged again by a shareholder in a 1960 case before the Tōkyō District Court[56], advancing largely the same arguments. The Court, using the same reasoning as the Ōsaka District Court, dismissed the plaintiff's arguments and no subsequent cases revisited the issue.

In 1964 the Supreme Court of Japan was asked for the first time to decide on a claim involving Article 269, a shareholder suit seeking the invalidation of a resolution that had approved a retirement bonus.[57] Two major questions were dealt with. The first was whether or not non-salary payments were included among the types of compensation that were covered by Article 269. The second was the extent to which resolutions could give discretion to the board while still complying with Article 269, the one in question having left most of the details, such as the amount to be paid and the timing and format of payment, to the discretion of the board. The Court clarified that in addition to salary other forms of compensation, such as

56 Tōkyō District Court, 5 May 1960, 判例時報 Hanrei Jihō 249, 31.

57 Supreme Court of Japan Second Petty Bench, 11 December 1964, 民集 Minshū 18, 2143.

retirement bonuses, had to be approved under Article 269. In upholding the original decision, the Court also held that while resolutions could be worded so as to give such broad discretion to the board, in order to satisfy the requirements of Article 269 this could not be interpreted as giving the board complete freedom when exercising such discretion. Rather it required the board to follow the company's standards developed through past practice when doing so. In this case those standards had included consideration of such things as the company performance, the years served and the personal accomplishments of the director. The decision was silent as to what would apply in situations where no such standards existed (companies not being required under the Commercial Code to create them), but the decision did establish that adherence to internal precedents based on logical standards, which as noted earlier forms a major cornerstone of executive compensation in Japan, was a prerequisite for meeting the substantive requirements of a resolution under Article 269.

c) Phase Two: Challenging Resolutions on Procedural Grounds

In the late 1960s shareholder cases began to also challenge resolutions approving pay based on procedural rather than substantive defects, an area where they would have more success. A notable 1967 decision of the Ōsaka High Court[58] involved a shareholder in the Ōmi Kenshi Bōseki Corporation, a textiles manufacturer, seeking a declaration declaring the non-existence or invalidity of a resolution that had approved a retirement bonus for several directors. The underlying cause of the dispute was the fact that one of these directors was the former president who at the time was under investigation by the Ōsaka prosecutor's office on suspicion of having embezzled a large amount of money from the company in a series of real estate transactions. The immediate legal claim, however, was based on the way in which the shareholders' meeting approving the resolution had been carried out.

The scandal implicating the president had received widespread media coverage and heightened interest in the shareholders' meeting, particularly among angry shareholders themselves. It also attracted the interest of organized crime. *Sōkai-ya* at the time were, and to a lesser extent continue today to be, a type of racketeer who earn money by extorting it through executives at scandal plagued companies. One of their preferred strategies was to buy shares in such companies and threaten to disrupt the shareholders' meeting unless they are bought off. One group of *sōkai-ya*, known as the Matsubakai, had purchased shares in the corporation specifically for this purpose.

58 Ōsaka High Court, 26 September 1967, 判例時報 Hanrei Jihō 500, 14.

Perceiving the threat of disruption by the Matsuba-kai, and also by legitimate shareholders wishing to air grievances, the new president (himself also implicated in the scandal) who was tasked with chairing the meeting decided to heavily stage manage it. This involved, immediately prior to the meeting, distributing shares to the employees of one of the company's subsidiaries. These were ordered to attend the meeting, sit at the front and applaud in unison when prompted. On the day of the meeting, 311 shareholders in total attended. Approximately 90 of these were employees of the subsidiary, a further 30 were believed to be *sōkai-ya* and the rest were (presumably) legitimate shareholders.

Chaos broke out almost as soon as the meeting began, with *sōkai-ya* rushing the stage each time the president attempted to introduce a resolution, upending tables, grabbing the microphone and committing a number of other disruptive acts. Each time the president and board members were forced to flee the room and wait for order to be restored. The police, who were in attendance, made several arrests of the worst offenders. In the midst of the bedlam, each resolution was passed with the president asking for applause and, on receiving acclaim from the employee-shareholders, recording each as accepted. Shouted questions and objections from other shareholders were ignored and no formal opportunity to ask questions was given.

The Ōsaka High Court held that the defects in the holding of the meeting were such as to justify an order invalidating the resolution approving the retirement bonus, thus marking the first shareholder success in a claim challenging one. The Court found that the employee-shareholders were a sham (the normal formalities for transferring the shares to them had not been carried out, meaning they had never actually owned the shares) and ignoring the formalities in the approval of resolutions during the meeting were severe enough as to meet the Art. 248 of the Commercial Code standard of being grossly unfair. The effect of this was to deny the retiring directors any legal claim to their retirement bonus.

d) Derivative Claims and the 1982 Commercial Code Reform

In the 1980s shareholder claims began to make use of other legal provisions to attack resolutions approving pay – particularly 1) derivative actions seeking to hold directors personally liable for breaching their duties in approving pay and 2) claims based on a 1982 amendment to the Commercial Code[59] which gave shareholders another tool to attack compensation-

59 On this amendment see generally M. E. FOSTER, Analysis of Newly Amended Commercial Code of Japan, Case Western Reserve Journal of International Law 15 (1983) 587.

based resolutions on procedural grounds without relying on the derivative action. In 1980 the Ōsaka District Court issued a decision (upheld on appeal by the Ōsaka High Court)[60] in a case in which a shareholder used a derivative action (contained in Article 267 of the Commercial Code) to seek to hold the directors of a company personally liable for a breach of their fiduciary duties and duty of care. The resolution in question was for a retirement bonus for some retiring directors which had been approved by the shareholders. The resolution had set an upper limit for the total amount to be paid to all of the directors, with the amounts paid to individual directors and other details like the timing of payment being left to the discretion of the board. In exercising this discretion, the board relied on its own internal rules for calculating retirement bonuses, which had been approved at a previous board meeting several years prior. The bonuses were then paid.

The plaintiff's main argument was that since the internal rules for calculating the bonus which the board relied on had not themselves been approved by the shareholders' meeting, the resolution approving the bonus was invalid and, having distributed the bonuses based on an invalid resolution, the directors who approved it had violated their fiduciary duties. Central to the argument was the idea that the internal rules, having been set by the board could be changed by the board and thus resolutions leaving it to their discretion could be arbitrarily used even when such internal rules existed.

The Court rejected the plaintiff's claim, but did acknowledge some of the concerns raised. It held that where a resolution approving pay and leaving certain details to the discretion of the board has been passed, the board was under an obligation to use whatever internal rules it had at the time of the resolution to implement it. Since the board had in fact used the internal rules which existed at the time of the resolution, the plaintiff's claim was dismissed. The High Court on appeal upheld this decision, but further elaborated on another concern which was whether or not the shareholders, at the time they approved of such a resolution, would have had knowledge of the internal rules. The Court acknowledged that in certain cases where the shareholders were unable to know of the existence or content of such internal rules, a resolution might be void. In the present case the rules had been recorded in the minutes of the board of directors meeting at which they were passed, a document which shareholders had a right under Article 263 of the Commercial Code to inspect, and thus it found that no such concerns existed.

60 Ōsaka District Court, 9 April 1980, 金商 Kinshō 603, 23; Ōsaka High Court, 29 October 1980, 判例タイムズ Hanrei Taimuzu 438, 159.

Closely following on this, in 1981 the Tōkyō District Court[61] would issue a decision in a similar case involving a shareholder seeking to hold directors personally liable to the corporation – Citizen Watch - for having approved bonuses and retirement bonuses that had been paid out, largely advancing the same argument as in the previous Ōsaka case. The resolutions had not specified the amount, but had said that it would be decided by the board in keeping with their contribution during their term and in accordance with customary practice at the company. One distinction with the previous case was that in this one the company had no written formula for calculating the amount of bonuses which could be accessed by shareholders using Article 263 and instead the amounts were calculated in accordance with precedent. The Court nonetheless dismissed the claim on the basis that the shareholders, having been given advance notice of the existence of the customary practice owing to its reference in the notification of convocation, had the opportunity to discern its substance through questions at the meeting.

In 1985 the Supreme Court of Japan, in a different case also involving Citizen Watch, issued a very brief one paragraph judgment[62] that clarified two important issues with respect to Article 269 of the Commercial Code and which would become an important precedent in subsequent cases. The first of these was affirming the, by then long standing, practice of allowing resolutions approving pay to identify a global amount to be paid to the entire board rather than requiring individual compensation for each director to be approved. The second was that it confirmed the scope of compensation covered. While all pay that directors receive in their roles as directors had to be approved by the shareholders, any compensation that they received for other duties (such as their roles as full-time employees for those that had them) were not. While their pay as employees had to be determined by a clearly established system approved by the board, it did not have to be subject to shareholder approval.

In the late 1980s shareholder claims once again began to rely on procedural challenges to resolutions approving pay, based on a 1982 amendment to the Commercial Code, a mechanism separate from the derivative action. Among the amendments was one to Article 237 which introduced a duty for directors to explain matters related to the resolutions being considered when asked by shareholders to do so, which previously they had not been under. In order to address the *sōkai-ya* problem the revision also strengthened the ability to remove disruptive shareholders from meetings.[63]

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61 Tōkyō District Court, 15 December 1981, 金商 Kinshō 648, 26.

62 Supreme Court of Japan Third Petty Bench, 26 March 1985, 裁判集民 Saiban Shūmin 144, 247.

63 FOSTER, *supra* note 59.

In 1988 the Tōkyō District Court issued the first decision[64] in a case relying on the new provision. A group of 93 shareholders in Bridgestone sought the invalidation of a resolution approving retirement bonuses for directors and *kansa-yaku* which had left the amount, timing and method of payment to the discretion of the board. At the shareholders' meeting one of the plaintiffs had asked the chairman of the meeting to disclose the amount to be paid. The chairman refused on the grounds that it was personal information and that there was no precedent for them doing that. The shareholder plaintiff then asked on what legal grounds the chairman was refusing to disclose the amount, to which the chairman refused to respond and instead, ignoring the plaintiff's objections, moved for a vote on the resolution which was then approved.

The court held that merely dismissing questions about the amount to be paid was not sufficient to comply with the duty to explain. Where resolutions are silent as to the amount but internal rules for calculating the amount exist, these must be disclosed and explained to the shareholder in response to such questions. Where the director is unaware of the content of such rules or requires further investigation, the reasons for this must be explained. Since the director had failed to do any of this in this case, the court allowed the plaintiff's claim and declared the resolutions approving the bonuses invalid.

The following year the Kyōto District Court issued a decision[65] in a similar case challenging a resolution approving a retirement bonus based on a failure of the director chairing the shareholders' meeting to comply with the duty to explain. In that case the exact amount to be paid, 90 million Yen, to a single director who was named, was stated in the resolution. The amount paid, however, was greater than what calculations based on the normal internal rules for retirement bonuses would have dictated. The plaintiff shareholder asked about this at the shareholders' meeting and was informed that owing to the important contributions of the director in question, who was the founder of the company, it had been felt that the normal rules for calculating the bonus were insufficient to recognize his contribution. In a back and forth exchange, however, the director was unable to elucidate any specific accounting method by which the amount had been arrived at.

The Court held that the duty to explain extended to all matters necessary for a shareholder to make a rational judgment about the resolution in question. Since the amount to be paid had been clearly stated in the resolution itself, the method by which the board had arrived at that figure was irrele-

64 Tōkyō District Court, 28 January 1988, 判例時報 Hanrei Jihō 1263, 3.

65 Kyōto District Court, 25 August 1989, 判例時報 Hanrei Jihō 1337, 133.

vant to the shareholder's decision about whether to support it or not. Despite the inability of the director to answer the plaintiff's questions at the meeting the court dismissed the claim since the information inquired about fell outside the scope of what the shareholder needed.

e) *The 1990s and 2000s – Corporate Governance Arguments, The Corporation as Plaintiff*

In the 1990s and 2000s shareholders continued to bring claims based on duty to explain violations with some success[66] and were joined by corporations themselves for the first time bringing claims against directors over compensation, often in response to shareholders' demands. Shareholder claims in this period began to exhibit arguments based on more nuanced corporate governance arguments, though courts have been reluctant to follow. In a 1998 Ōsaka District Court case[67] the plaintiff shareholder sought to overturn the established precedent on allowing the details of bonuses to be left to the discretion of the board subject to its internal rules. The company in that case was mired in a widely publicized scandal and the plaintiff noted that allowing the directors to determine the details of bonuses based on rules that had been approved prior to such scandals or negative performance information coming to light placed severe limits on the abilities of shareholders to use pay as a way of disciplining directors. The Court, repeating precedent from earlier cases, dismissed the claim.

Similarly in 2005[68] the Tōkyō District Court was asked by a shareholder, in a derivative action seeking personal liability against the directors, whether it constituted a violation of the director's fiduciary duty to fail to submit an Article 269 resolution to the shareholders seeking a reduction in their pay when the company has gone into the red. The Court held that the duty did not require that, noting that the proper remedy was for a shareholder to introduce a shareholders' resolution demanding a reduction in pay.

Claims brought by corporations against directors begin to appear in this period and have appeared with some frequency since 2000. The legal basis for them differs significantly from those brought by shareholders. Such claims are generally brought against former directors seeking repayment of compensation that is alleged to have been wrongfully paid. Many of these claims are advanced under the Civil Code provision on unjust enrichment (Article 703) or its general tort provision (Article 709). Often at issue in these cases is the question of whether the remuneration at issue had been

66 For example Nara District Court, 29 March 2000, 金商 Kinshō 1090, 20.

67 Ōsaka District Court, 18 March 1998, 判例時報 Hanrei Jihō 1658, 180.

68 Tōkyō District Court, 30 May 2005, Westlaw Japan 2005WLJPCA05300007.

properly approved under the requirements of the JSOP rule. Most of these cases involve smaller privately held corporations where formalities are often not observed and in a number of cases the Courts have allowed claims on the basis that the director's pay had not been properly approved by the shareholders. At the same time however, mindful of the hardship this might create the Courts have also relied on the general Civil Code provisions on good faith and abuse of right to place some limits on such claims. The Supreme Court in 2009[69] held that such claims by the corporation constitute an abuse of right where the company waits more than a year to bring a claim. Similarly, in a 2018 case[70] the Tōkyō District Court dismissed a claim brought against a director in a family owned company for several years of pay he had collected without a shareholders' resolution approving it on the basis that given the totality of the situation – he had actually worked and the shareholders had known he was being paid for it throughout the period at issue – the claim constituted an abuse of right.

f) The Re-delegation Problem and the 2018 U-Shin Case

In 2018 a particularly noteworthy shareholder derivative action brought to the Tōkyō District Court[71] (whose decision was later upheld by the Tōkyō High Court)[72] highlighted a significant long running problem related to the delegation (and re-delegation) of authority to make compensation decisions. The problem can put an extraordinary amount of power in the hands of the representative directors, in corporations organized under the companies with *kansa-yaku* system that most use, over how each individual director is paid, including themselves, which gives them the ability to distribute the amount in extremely unequal ways. In that case the shareholders of U-Shin, an auto parts maker listed on the Tōkyō Stock Exchange, had passed a resolution approving an increase in the compensation limit for all directors from 1 billion to 3 billion Yen, delegating authority to the board to decide how individual directors would be paid. The board of directors met immediately after the shareholders' meeting and passed a resolution of their own delegating that authority in turn to the representative director. The representative director shortly thereafter used that authority to grant himself compensation of over 1.4 billion Yen (approx. 11 million Euro) for the year. This constituted almost the entire amount paid to the board as a whole

69 Supreme Court of Japan Second Petty Bench, 18 December 2009, 裁判集民 Saiban Shūmin 232, 803.

70 Tōkyō District Court, 22 January 2018, 判例タイムズ Hanrei Taimuzu 1461, 246.

71 Tōkyō District Court, 12 April 2018, 金商 Kinshō 1556, 47.

72 Tōkyō High Court, 26 September 2018 金商 Kinshō 1556, 59.

(a little over 1.6 billion Yen) and instantly made him one of the highest paid corporate executives in Japan.

Dissident shareholders brought a derivative action against the representative director and the rest of the board for breaches of their duties in respect of the pay decision. Their arguments were largely based on the fact that the explanations given for the raise in compensation limits to the shareholders' meeting had stated that it was based on a recent acquisition of a new division from a French company. This acquisition was predicted to require a future increase in the number of directors and also in their duties and responsibilities which might necessitate raising the pay of the board as a whole, though there were no immediate plans to do so and any changes would be made in light of sales and profit at the relevant time. Despite this assurance, the representative director's pay had been substantially increased very shortly thereafter without any increase in the number of directors (whose pay other than his remained largely unchanged) or any improvement that would justify it. Thus, they argued that the representative director's decision violated the intention of the shareholders' meeting when it passed the resolution. They also argued that irrespective of the explanations, the representative director had a duty to exercise his authority to set his own pay at a reasonable level which he had breached. Evidence from internal discussions among the board members and the company's head office indicated that one of the animating concerns driving the discussion leading up to the decision was simply determining the maximum amount he could increase his own compensation by given the legal and business limits that existed.

The Court dismissed the claim. Citing precedent it noted that the re-delegation of authority to make decisions on pay in this manner – from the shareholders' meeting to the board of directors to the representative director – was not a violation of Article 361 of the Companies Act so long as the ultimate decision respected the upper limit set by the shareholders. It held that while representative directors in exercising that delegated authority had to abide by their fiduciary duty and duty of care, the business judgment rule afforded them a very broad range of discretion in making decisions. Except for when either the process leading to the decision or its content were shown to be clearly unreasonable, such decisions would not constitute a violation of the director's duties. Looking at the decision in question it found that the representative director had informed himself of the various risks associated with his pay to the company and modified his pay level accordingly, while at the same time the business was improving as a result of the acquisition. In light of these it held that the decision could not be said to be clearly unreasonable and thus did not constitute a violation of his duties. In light of this it further held that the rest of the board had likewise not breached their duties. The standard used suggests that so long as a representative director can find some rational basis to justify their pay and how they divided the amount authorized by the shareholders among the members of the board the Courts will defer, even in cases where they exercise that to give almost all of it to themselves. This issue is further illustrated in, and may also explain the prevalence of, director lawsuits seeking pay, which we now turn to.

6. *Defending Director Pay: Director Litigation*

a) *Background*

While the above developments were taking place in the field of shareholder and corporate litigation a parallel story was being developed with regard to a distinctively different set of claims relying on the same provision: director claims for compensation. The set of questions which the courts were forced to answer, and the related legal provisions, were quite different than those in shareholder and corporation claims.

One of the earliest decisions, a 1968 case before the Ōsaka High Court[73], outlines one of the initial fundamental problems that had to be dealt with, which was when a director's legal claim to any compensation came into existence. Article 254 of the Commercial Code stated that directors are subject to the rules on mandate contained in the Civil Code, Article 644 of which states that mandatories absent an agreement to the contrary do not receive compensation for their work. Thus, in order for a director to have a legal claim to compensation the director must prima facie prove the existence of an agreement affirming such a right. The Court in this case, which involved the representative of the estate of a deceased director advancing a claim against the corporation for unpaid base pay, bonuses and retirement bonus, overcame this by flipping the assumption on its head when it came to corporate directors. Absent evidence that it was intended to be an unpaid position, the court held that there was an implied term in the contract between directors and the corporation that it was to be a paid position.

The existence of such an implied term was not, however, enough in itself to establish a director's legal claim to compensation. It still had to comply with Article 269 of the Commercial Code and be approved by either a shareholders' resolution or in the articles of incorporation. The pay at issue in this case had not been approved by either, the plaintiff instead advancing the claim on the basis that the director (his father) should have received the same compensation as paid to other directors at the same time. The court rejected this, holding that the lack of approval under Article 269 formed a solid bar to any claim for director compensation.

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73 Ōsaka High Court, 14 March 1968, 金商 Kinshō 102, 12.

b) The Battles of the Retirement Bonuses 1: Shareholder Resolutions versus Contractual Obligations

Many subsequent director cases illustrate how this requirement could put their claims for pay not just at the mercy of shareholders but also of their fellow directors, and introduced an element of uncertainty into their contractual claims. In particular this related to the practice of making retirement bonuses a major component of the overall pay package directors (and most employees) received. As noted earlier these retirement bonuses fell within the type of compensation which had to be approved by the shareholders under Article 269 of the Commercial Code, meaning that when a director retired a resolution approving their retirement bonus would have to be put to the shareholders' meeting for approval.

A Kyōto District Court decision from 1969[74] illustrates the problem this created for directors. The plaintiff in that case was a retired director suing the corporation for a 3 million Yen (approx. 384,340 Euro) retirement bonus he claimed to have been entitled to. The representative director, a position that allows one to make contractual commitments on behalf of the corporation, had promised the bonus to the director, but ultimately the company reneged on that and paid a much smaller retirement bonus. The director, however, faced an insurmountable hurdle – the board had never submitted a resolution to the shareholders' meeting seeking approval of the retirement bonus. A director's legal claim for compensation of any kind only comes into existence when it has been approved in accordance with Article 269 and since no approval had taken place the director's claim was dismissed.

This seems to have created a mechanism for ensuring loyalty of directors and of punishing misbehavior. Since the board is not under any obligation to put a resolution to the shareholders to begin with they can use this as a means of denying bonuses to directors forced out due to scandals or simply for having been on the losing side of an intra-board power struggle.[75] Even when the board does put a resolution for a retirement bonus to the shareholders it still has a great deal of discretion as to how much it asks for on behalf of the director. Any internal rules for calculating bonuses a company has, or past practice, is generally subordinated to the contents of such resolutions. In a 2003 Tōkyō District Court case[76] a former director brought a case against the company and its directors in relation to a retirement bonus he had received. The director in question had been one of several who had involved the company in a bad debt problem which had a serious negative

74 Kyōto District Court, 16 January 1969, 判例タイムズ Hanrei Taimuzu 232, 164.

75 See Tōkyō District Court, 27 December 2010, Westlaw Japan 2010WLJPCA 12278004, for one such case.

76 Tōkyō District Court, 27 June 2003, Westlaw Japan 2003WLJPCA06270007.

impact on the company. His retirement bonus had been approved by a shareholders' resolution which specifically stated that owing to his personal responsibility for the company's problems the board would not follow the established internal rules for calculating the bonus, which in the result was set at a level approximately 40% of what it normally would have been. The director raised a number of arguments challenging the resolution, in particular the fact that by allowing the board to be unbound by the internal rules essentially left it at its complete discretion. The Court rejected the plaintiff's argument, holding that the resolution was valid as it did not purport to give unfettered discretion to the board but merely to provide a bonus less than what the internal rules would normally require. Other cases have upheld similar resolutions approving lower retirement bonuses than what the internal rules would normally dictate for reasons not related to the director[77] and firmly established that the existence of internal rules in and of itself does not create a legal claim to pay in the absence of the approval required by Article 269 of the Commercial Code.[78]

The Courts have on occasion placed limits on the ability to use the lack of a resolution approving pay to deny a director a retirement bonus, but these have been limited to cases involving closely held corporations in which it could be shown that all of the shareholders had consented to the compensation even though the formalities of a shareholders' meeting had not been carried out.[79]

c) Battle of the Retirement Bonuses 2: After the Shareholder Resolution

While the requirements of the JSOP rule place directors at a distinct disadvantage prior to a resolution approving their retirement bonus has been put to the shareholders and approved, once that takes place their legal position improves substantially. While such resolutions generally require the board of directors to follow through by exercising whatever discretion the resolution leaves them in setting the bonus, they are under a positive duty to give effect to it. They can no longer defer as a way of punishing a disfavored director. In a Tōkyō District Court decision[80] a retired director brought a suit against the corporation and five of its directors for breaches of their duty of care and fiduciary duty for having failed to give effect to a shareholder resolution approving his retirement bonus. The resolution left the details of the bonus to the discretion of the board, which ultimately failed to

77 Such as bad business: Tōkyō District Court, 27 September 2002, Westlaw Japan 2002WLJPCA09270011.

78 Ōsaka High Court, 12 February 2004, 金商 Kinshō 1190, 38.

79 Kyōto District Court, 27 February 1992, 判例時報 Hanrei Jihō 1429, 133.

80 Tōkyō District Court, 20 December 1994, 判例タイムズ Hanrei Taimuzu 893, 260.

approve any bonus. This was due to an accounting scandal that had erupted at one of the company's shipyards which the plaintiff had failed to prevent. The Court held that the directors' duties required them to implement the resolution, which made no mention of the scandal, within a reasonable time and their failure to do so constituted a breach of such.

d) *Battles for Other Compensation*

The fact that retirement bonuses are the type of compensation most litigated by directors is likely a result of the fact that there is almost always an individual director's name attached to a resolution approving it since they only become necessary on that individual's retirement. Other resolutions approving different kinds of pay (such as base salary, stock options or annual bonuses) are generally approved for the board as a whole rather than for any identified individuals, with the division of the total amount approved among directors left to the discretion of the board.

Despite this, some cases have also looked at these other types of resolutions, particularly in terms of director claims to base salary. Resolutions approving base salary set a limit on how much all directors can cumulatively be paid rather than defining how much each will actually be paid (which is left to the board's discretion within that limit). These do not have to be set each year, but only when a change to a previously established limit is desired. This can create confusion in regards to the content of a director's legal claim to salary.

In claims related to base salary, the courts have generally created strong protections to the director's right to salary once a resolution approving it has been passed. As with retirement bonuses there have been attempts by those controlling the board to cut the base salary of disfavored directors as a form of punishment, but courts have generally stepped in to prevent this sort of activity. In a 1997 Nagoya District Court decision[81], the shareholders' meeting had passed a standard resolution approving a global limit to the salary for all directors, leaving the details on how it was to be distributed to the board. The board in turn had set the individual pay of two directors (the plaintiffs in the case) at 1.7 and 1.13 million Yen (approx. 13,000 and 10,000 Euro respectively) per month. Not long thereafter an internal power struggle within the board resulted in one faction ousting the representative director and replacing him with their candidate. The two plaintiff directors had opposed this move. At a subsequent board meeting it was decided to change their status from full time to part time directors and leave decisions on their base salary to the discretion of the new representative

81 Nagoya District Court, 21 November 1997, 判例タイムズ Hanrei Taimuzu 980, 257.

director, who set it at 100,000 Yen (approx. 780 Euro) per month. Neither director had consented to this and sued.

This was a very rare case since the two plaintiffs were still directors of the company, but the Court held that their bringing the claim did not constitute a violation of their duties. The Court held that once a director's pay level is set by the board within the limits set by the shareholders, it creates a binding legal claim to that pay. Since it is a contractual claim, it cannot be altered unilaterally by one party to the contract without the other's consent and so the directors in this case were entitled to their salary as it had been originally set.

The Court in that case relied on a 1992 Supreme Court of Japan decision[82] which had in fact defined the director's right to salary even more strictly. In that case rather than the representative director attempting to similarly cut the base salary of a director who had fallen out of favor, the board had put a resolution before the shareholders' meeting which stated that the director's position was to be turned into an unpaid one. This was done without the director's consent and the court held that a director's claim to salary once it has been approved cannot be unilaterally altered, even via a subsequent shareholders' resolution purporting to do the same.

While a director's claim to base salary is thus protected from unilateral changes, the content of their claims can sometimes be unclear as illustrated in one 1980 Fukuoka High Court case[83] in which a director who had been forced to resign after a scandal sued the company for one year's worth of base salary he had not been paid. Complicating the case was the fact that the board had in that year allocated pay to each director which cumulatively exceeded the limit approved in the most recent shareholder resolution, which at that point was 20 years old. Since it was impossible for the Court to decide which director's pay had exceeded the total, it resolved the conflict by recognizing the retired director's claim to a pro-rata share what his relative salary would have been had the board complied with the shareholders' resolution.

V. DISCUSSION: THE COURTS AND DIRECTOR COMPENSATION IN JAPAN

What do we learn from the above developments about the role of the courts with respect to director pay in Japan? With respect to the descriptive question, four points suggest themselves as worthy of note. The first is that the Courts are quite active in director pay disputes in Japan, despite the exten-

82 Supreme Court of Japan Second Petty Bench, 18 December 1992, 民集 Minshū 46(9), 3006.

83 Fukuoka High Court, 31 January 1980, 判例時報 Hanrei Jihō 969, 106.

sive body of literature mostly devoted to explaining how little use Japanese society has for them.[84] Given the increase in corporate litigation in general since the 1990s however, this is perhaps unsurprising.[85] The second point is that the cases evidence a much more diverse pattern of litigation than the prototypical shareholder derivative action that dominates the American literature. Cases related to directors' duties are relatively rare and instead most cases, regardless of the nature of the claim or who brought it, turn on the question of whether the various formalities of the JSOP rule (many of which developed by the courts) have been complied with. Third is that the courts are used with much more frequency by directors themselves seeking to enforce their pay rather than shareholders looking to challenge it, to the extent that the courts could perhaps more accurately be described as primarily a mechanism for directors to enforce their claims to pay rather than one for shareholders to challenge it. Given the purpose of the JSOP rule this is a curious finding. It is partly explained by the fourth observation, which is that the courts have allowed a practice of approving pay in compliance with the JSOP rule to develop which has placed an extraordinary amount of power to make decisions on pay not in the hands of shareholders but rather in the hands of boards and representative directors who dominate them. This in turn has introduced some risk into the entitlements of directors with respect to elements of their pay, particularly retirement bonuses, which explains their frequent recourse to litigation.

While the system thus fashioned is difficult to understand in the framework of the American literature on courts, where the need to police pay to ensure the interests of executives are adequately aligned with the corporation and its shareholders is the main concern, when we consider them in the overall Japanese context outlined in section III above it can be said that it complimented the approach to director pay that companies developed over the post-war period. While the courts explicitly interpreted the JSOP rule as being intended to prevent directors from abusing their ability to set their own pay by empowering shareholders, in fact the rules devised gave the board so much discretion that it made effective use of the tool by shareholders difficult in litigation, for the most part funneling disputes into claims against the resolutions themselves, focusing on whether their pro-

84 Notably started by T. KAWASHIMA, Dispute Resolution in Contemporary Japan, in: von Mehren (ed.), Law in Japan: The Legal Order in a Changing Society (1963) 41. For a more recent account which provides an overview of how the debate evolved over time, see COLOMBO / SHIMIZU, *supra* note 48.

85 On the rise of shareholder derivative suits in particular see D. PUCHNIAK / M. NAKAHIGASHI, Japan's Love for Derivative Actions: Irrational Behavior and Non-Economic Motives as Rational Explanations for Shareholder Litigation, Vanderbilt Journal of Transnational Law 45 (2012) 1.

cess of approval or substantive content met the standards which the court defined. At the same time, however, the system created was perfectly compatible with Japan's employee-centered system of corporate governance. By subjecting the contractual claims of directors to the discretion of the board or the representative director, they were empowering the board – an organ made up of employees, much more likely to share their normative views on pay than outside shareholders and itself subject to a great deal of internal monitoring – as the gatekeeper for policing pay. This subjected directors to contractual claims that were much weaker than anything American executives would be familiar with and allowed the board to use its power over pay as a disciplinary mechanism when misbehavior by individual directors was uncovered. While the courts did not give the board completely unfettered discretion – requiring it to follow proper procedures during the approval of resolutions and strictly protecting individual directors' pay once legal claims have crystallized – these did not fundamentally undermine the broad discretion granted to the board in using pay as a disciplinary mechanism. At the same time however, this wide degree of discretion, which in some cases have allowed representative directors to make distributive decisions about the pay of their board that seem widely at odds with prevailing norms with few limits, as illustrated in the 2018 U-Shin case, suggest that this system is coming under tension.

From the perspective of the normative question, how do we evaluate this role? This would obviously depend on which side of the fence one sits. Within the overall institutional context those who are critical of efforts to implement aspects of American practice owing to concerns related to income inequality might praise the court's role in allowing the traditional pay system to develop, which in some ways was dependent on how the courts chose to apply the rules. They might also note a certain irony in the fact that a rule designed specifically to put a check on director pay has mainly found its way to court via cases brought by those same directors seeking to enforce their claims to pay. Conversely those advocating a shift to greater reliance on incentive-based pay might find the paucity of successful shareholder derivative actions and the overall structure of rules developed less appealing.

VI. CONCLUSION

This paper has examined the case law on director compensation disputes in Japan based on the provision in the Commercial Code (Article 269) and later Companies Act (Article 361) regulating director pay. From what we learn from the cases we can draw several conclusions. To begin with, litigation of director pay disputes seems to be relatively common in Japan, with at least 230 judicial decisions existing that are based directly on such disputes. These disputes are quite different than the prototypical cases envisioned by the debate on litigation's role in executive compensation in the United States, reflecting the significantly different content of the legal rules and differences in the broader systems of corporate governance.

The Japanese courts have, in handling these cases, played an important and hitherto unappreciated role in defining the rights and duties of shareholders and directors in a way that is largely complimentary of Japan's employee-centric model of corporate governance and the pay related norms that have developed alongside it. It has taken a rule purportedly intended to benefit shareholders and turned it into a tool by which the board of directors and in some cases representative directors can use the broad discretion courts have granted to exercise internal discipline over board members using pay. The board, as a body made up largely of employees and normatively bound to their interests is perhaps better suited to this function than the shareholders' meeting. This suggests that the courts have in granting the board the discretion it has (none of which is envisaged by the wording in of the JSOP rule) played an important role in developing Japan's system of director compensation.

How we evaluate that role from a normative perspective is a more difficult question and may largely coincide with an evaluation of the overall system. On the one hand it has contributed to keeping executive pay levels relatively modest in international comparison, allowing Japan to avoid the negative consequences associated with executive excess seen in jurisdictions like the United States and elsewhere. On the other hand, reforms within Japan in recent years, within the context of larger scale changes to corporate governance in general, have explicitly sought to more closely align pay practice at large corporations with standards that major international institutional investors are familiar with. While this may have the benefit of making Japanese companies more attractive to such investors, it also risks undermining this more egalitarian pay system.

On a concluding note, at the time this study was written the effects of many of these reforms – including to the Companies Act and Japan's Corporate Governance Code – were too recent to be reflected in the case law. The questions of how they will affect the trends in litigation described, and what impact it might have on Japan's system of director compensation, are ones that are likely to be worth re-visiting in a few years' time.

SUMMARY

This paper reviews a set of 230 judicial decisions collected by the author which were rendered by Japanese courts in disputes over claims of corporate direc-

tors to their pay between 1953 and 2018 in order to investigate what role the courts have played in relation to Japan's executive compensation practices. These all centered around either Article 361 of the Companies Act or its predecessor Article 269 of the Commercial Code, the main rule governing director compensation. The paper makes four findings which shed light on this question.

The first is that Japanese courts, and particularly the Tōkyō District Court, deal with director compensation disputes quite frequently. This has particularly been the case since the turn of the century, with decisions appearing at a rate of roughly ten per year since 2000. The second is that the nature of these litigated disputes differs drastically from that described in the literature on executive compensation and the courts, which is largely based on American experience and focuses on shareholder use of derivative actions to challenge pay decisions. Article 361 of the Companies Act can be loosely described as a type of "Say on Pay" rule, which requires the pay of the board of directors be set either in the articles of incorporation or by a resolution of the shareholders' meeting. This procedural requirement has lent itself to a fairly diverse set of uses in the Courts. Broadly speaking these fall into one of two categories. On the one hand, in keeping with its purpose, the rule has been used by both shareholders and corporations themselves to challenge director entitlements to pay, though shareholder claims rarely take the form of derivative actions. On the opposite side it has been used with even greater frequency in lawsuits initiated by directors claiming remuneration from corporations. A third insight which follows from the second is that in Japan with respect to director pay litigation in the Courts could more accurately be described as a mechanism for directors rather than shareholders. The vast majority of cases which this study uncovered are in fact lawsuits initiated by directors seeking to enforce claims for remuneration against the corporation, with shareholder lawsuits being far less common. The reason for this lies primarily in the fourth and final insight, which is the important role the courts have played in developing the rule itself. Taking a provision that consisted of a single line which left an enormous number of issued unanswered the Courts developed a fairly extensive set of rules governing how it, and by extension how decisions on director pay, operated. In particular the cumulative effect of these has been to give boards of directors, and particularly the representative directors who exercise control over them, a great deal of independent power to set the pay of individual directors which has served to enhance the role of the board as a "gatekeeper" with respect to pay. This in turn has put the pay of individual directors, and particularly those who run afoul of the representative directors, at some risk which has led many to turn to the courts to try to enforce their claims.

ZUSAMMENFASSUNG

Der Beitrag analysiert 230 Entscheidungen japanischer Gerichte, die zwischen 1953 und 2018 in Verfahren ergingen, in denen um die Vergütung von Verwaltungsratsmitgliedern von Unternehmen gestritten wurde, um auf diese Weise zu klären, welchen Einfluss die Gerichte auf die Vergütungspraxis in Japan bislang gehabt haben. In sämtlichen Entscheidungen ging es um die Interpretation des Art. 361 Gesellschaftsgesetz bzw. dessen Vorgängernorm Art. 269 Handelsgesetz a.F. Die Untersuchung kommt zu vier Schlussfolgerungen, die zur Klärung der Frage beitragen.

Die erste Beobachtung ist, dass japanische Gerichte, insbesondere das Distriktgericht Tōkyō, sich relativ häufig mit Streitigkeiten wegen Vergütungen von Verwaltungsratsmitgliedern befassen. Eine zweite Beobachtung ist, dass sich diese Streitigkeiten in ihrem Wesen deutlich von denjenigen unterscheiden, welche das allgemeine Schrifttum zu dieser Frage behandelt, das stark von US-amerikanischen Erfahrungen geprägt ist und sich entsprechend auf den Einsatz von Aktionärsklagen zur Überprüfung von Vergütungen konzentriert.

Art. 361 Gesellschaftsgesetz lässt sich grob als eine Art „Say on Pay" Regel umschreiben, nach der die Vergütung des Verwaltungsrates entweder durch die Satzung des Unternehmens oder durch die Hauptversammlung festgesetzt sein muss. Die Gerichte haben dieses organisationsrechtliche Erfordernis in recht unterschiedlicher Weise interpretiert. Generalisierend kann man sagen, dass von der Regelung bisher in zwei unterschiedlichen Konstellationen Gebrauch gemacht worden ist. Zum einen haben Aktionäre und auch Unternehmen die Regel genutzt, um die Vergütungsansprüche von Verwaltungsratsmitgliedern überprüfen zu lassen, wobei Aktionärsklagen nur eine geringe Rolle gespielt haben. In wesentlich größerem Umfang haben zum anderen aber Verwaltungsratsmitglieder selber die Regelung in gerichtlichen Verfahren genutzt, um ihre Vergütungsansprüche gegenüber den Unternehmen durchzusetzen.

Eine dritte Beobachtung, die aus der vorhergehenden folgt, ist diejenige, dass gerichtliche Streitigkeiten über Vergütungsfragen in Japan überwiegend von Verwaltungsratsmitgliedern und nur in geringerem Umfang von Aktionären als Mittel zur Klärung von Vergütungsfragen genutzt werden. Bei den allermeisten der für diesen Beitrag untersuchten Klagen handelt es sich um solche, die von Verwaltungsratsmitgliedern erhoben wurden. Der Grund hierfür liegt vor allem in der aktiven Rolle, welche die Gerichte in der Ausdifferenzierung der Regelung gespielt haben. Dies ist die vierte und finale Analyse des Beitrages. Da die Norm äußerst knapp gefasst ist und entsprechend zahlreiche Fragen unbeantwortet lässt, hat die Rechtsprechung eine Reihe von Grundsätzen zu deren Anwendung entwickelt, unter anderem bezüglich der Frage, wie die Entscheidung über die Vergütung zu treffen ist. In ihrer Gesamtheit haben die gerichtlichen Vorgaben dem Verwaltungsrat – und damit faktisch dessen

vertretungsberechtigten Mitgliedern, welche diesen kontrollieren – einen großen Ermessensspielraum bei der Festsetzung der Vergütung im Einzelfall eingeräumt. Im Ergebnis hat dies die Rolle des Verwaltungsrats als „Gatekeeper“ im Rahmen von Vergütungsfragen gestärkt. Das wiederum hat Vergütungsrisiken für die einzelnen Verwaltungsratsmitglieder mit sich gebracht, vor allem wenn es zu Auseinandersetzungen mit dem Unternehmen kommt. In derartigen Situationen haben sich die Betroffenen oftmals an die Gerichte gewandt, um ihre Vergütungsansprüche durchzusetzen.

(Die Redaktion)