KÜRZERE ABHANDLUNGEN
SHORT ARTICLES AND COMMENTS

Shareholder Capitalism Comes to Japan

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Much discussion of corporate governance is what one might call Platonic-revelatory, what Popper called essentialist. That there is such a universal as "good corporate governance" is taken for granted. The job of the scholar or guru is to define what it is and reveal its implications, much as Plato pursued the essence of truth and beauty. In fact, of course, there is no model of an essential or proper form of capitalism which the law should embody. Company law in any country is the product of clashing domestic interests and ideologies, within the framework of that country's modal political values and cultural predispositions.

The current debate about corporate governance in Japan revolves around two axes: the nationalist axis sets the desirability of introducing changes seen as conforming to global, i.e., American, standards against the desirability of preserving valuable elements of Japanese tradition. The second, the class axis, is about framing the law to give pre-eminent consideration to the interests of owners vs. retaining substantial rights for employees. In the former dimension, Enron and World Com have led to some reversal of Americanising trends, but the shift in institutions and ideology on the second dimension has been, and continues to be, one way – emphasising the power and interests of shareholders. It is no exaggeration to say that a quiet shareholder revolution has taken place in Japan.

The first half of 2006 saw practically every magazine in Japan and countless television programmes featuring articles and documentaries on *kakusa mondai* – widening income inequality. Extraordinarily, the debate seems to involve no reference to this shareholder revolution in spite of the probability that, as over the last quarter-century in the United States, its long-term consequence will be a growing gulf between rich and poor. "Managers need to give consideration to all stakeholders and not just shareholders" has recently become common rhetoric among leading industrialists. It needs to be given institutional reinforcement in company law if it is to be more than hypocritical rhetoric. I make some concrete suggestions in that regard towards the end of this paper.

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* For a fuller discussion of the views expressed in this paper see R. DORE, *Dare no tame no kaisha ni suru ka* [Who should we make the corporation for?] (Tokyo 2006).

The nature of corporate governance best revealed in crisis.

The crucial aspects of a country's corporate governance system – in Lenin's term, the "who whom" of corporate governance – best shows up in times of crisis: e.g., when someone tries to get rid of the CEO or when there is a hostile takeover bid. It is instructive to compare three examples of ousting a CEO: "Chainsaw" Dunlop from Sunbeam, Shigeru Okada from Mitsukoshi, and Takao Okuma from Okuma Machine Tools. The first was a case of summary dismissal by external directors heavily invested personally in Sunbeam in response to an alarming fall in the share price. The second came as a result of a shift in the CEO's internal and external reputation finally only catalysed in a board vote to dismiss by the moral suasion of the one outside director, a representative of the store's main bank. The third was also the result of a growing conviction within the firm that the CEO cared more for his family than for the firm and was catalysed by the employee union's strike threat. The first exemplifies what I propose to call the "shareholder property model" of the firm – the view that the firm is an instrument for its owners' profit. The other two exemplify what I propose to call the "quasi-community model" of the firm, the view that the firm is a community of people who are committed to work in it, run by its elders who are primarily concerned with the reputation and future prosperity of the firm and the welfare of its members.

The difference ought to show up much more clearly than it does in the current Japanese debate about hostile takeovers. Neo-classical economists take the shareholder property model for granted, and claim that takeovers are an essential element of market discipline which harnesses greed and fear to improve the efficiency of managers in the use of scarce resources and consequently enhances general welfare. Take apart the underlying assumptions of this argument – e.g. that a company's share price represents the present value of the discounted stream of future earnings as estimated by the best-informed analysts – as well as studies of the efficiency effect and the welfare effect of takeovers in other societies, and the hollowness of the argument is obvious, but, though institutional economists have constantly made such arguments elsewhere, such rebuttals seem to be rarely heard in consensus-loving Japan.

Global standards and the social infrastructure of corporate governance

The currency of definitions of corporate governance which effectively restrict it to relations between owners and managers is a function of the global cultural dominance of the anglophone world, a dominance such that Czechs, Japanese and even French seek to put their corporate governance theorising in English. German institutions in which employees have strong legal rights and Japanese institutions in which they had strong conventional rights are treated, in footnotes, as aberrations.

A more encompassing definition would concentrate on power and its distribution – who can coerce, or is in a better position to persuade, whom to do what, and to determine who gets what in the distribution of the value which the firm adds to its inputs.

Corporate governance is not like the metric system. There is no compelling reason for global uniformity – compelling, that is, to anyone other than members of the global finance industry. National variation has two sources. One is political values – the national bias to social democratic or neo-liberal ideologies – compare the German with the American system. The other is the level of generalised trust. Some degree of "institutionalisation of suspicion" in forms of accountability is necessary anywhere, but the extent to which one can chiefly rely on managers' consciences for honest and competent management, or alternatively needs to carry the "everybody is a potential crook" assumptions to Sarbanes-Oxley proportions varies from country to country. Japan is still, though diminishingly so, blessed with a business culture with reasonably robust consciences and levels of personal trust.

Why reform in Japan?

There has been a veritable flurry of reforms of corporate governance, culminating in the major company law revision of 2002 and its consolidation in the 'colloquial" revamp of 2005. All were reforms which brought Japanese legal institutions closer to those of the United States. What has inspired them? The reasons usually offered cry out for a sceptical look: corporate scandals, indecisive management, loss of innovative capacity, overinvestment, low returns to capital, and neglect of shareholders. I believe that the true reasons were: the loss of the national self-confidence induced by thirty years of high growth performance and with it the loss of pride in "truly Japanese" institutions, secondly, the arrival to positions of influence in the governmental, academic and corporate bureaucracies of the "brainwashed generation" of American-trained MBAs and PhDs, and thirdly the growth of foreign ownership of Japanese equities from 5% in 1990 to close to 25% today.

What reforms?

The legal changes, in spite of their declared intentions to rectify the disempowerment of shareholders, on the whole greatly increased managerial autonomy more than they enhanced shareholder power. It is significant that only a small minority of firms have availed themselves of the option of an external-director-dominated committee system of governance offered in the 2002 law revision, and many of those for reasons which have nothing to do with the motives of the drafters of the legislation. There have also been other changes in board structure much more widely diffused and not required by any legislation – slimming down of the main board and the creation of a posse of "executive officers", appointment of two or three external directors or creation of an advisory board etc. In the light of the arguments for these changes, one is entitled to ask whether they have made decision-making more efficient, more speedy, and less likely to lead to illegal or anti-social enterprise behaviour. My conclusion is that the answers are, respectively, marginally, not at all, and marginally.

Shareholder power

The exercise of voice and the threat of exit are best considered separately. Most subsidiaries, of course, have a dominant share-holding parent and the new rules of consolidated reporting make sense. The banks and insurance companies which once held significant but still modest holdings of independent companies always were restrained in their monitoring except when the firm was in real trouble. That is still the case though banks have had greatly to reduce the size of their holdings. They seem, however, to have done so because they had to, not as a profit-making strategy à la Deutsche Bank. The new dominant shareholder is the private equity/buy-out fund. Steel Partners is the most famous of a dozen American funds which acquire a 10-15% holding and then use the threat of take-over to shake down some under-priced cash-rich smallish firm. The Murakami fund, the most prominent of the indigenous operators of this species, came down in a spectacular crash when prosecutors, widely believed to be motivated by a general aversion to "money-game" operations, chose its owner for a rare indictment of insider trading.

As for minority shareholders, their voice in AGM voting and bringing or threatening derivative suits is gradually being organisationally consolidated by three organisations of institutional investors (ISS for foreigners, Japanese pension funds and the equity investors association of trust banks etc.) and also by one Nader-like association of public-spirited citizens. These have succeeded in making some waves (on disclosure of directors' salaries for example) and AGMs have become slightly more lively affairs; they lasted on average for 48 minutes in 2005 compared with 29 minutes in 1993.

But the chief way shareholder power has been enhanced is by the fact that shareholder exit and a fall in the share price is no longer the matter of indifference to managers that it once was. The threat of takeover has become real. Keeping up the share price has shot from ninth or tenth in the traditional survey list of managerial objectives to the top. This is the real source of the shareholder revolution.

Active discussion of anti-takeover defences started in 2004 in METI (Ministry of Economy, Trade and Industry), originally with a clear "fear of foreign takeover" inspiration *à la francaise*. All nationalism was bled out of the proceedings, however, (Koizumi has promised the Americans a doubling of foreign investment in Japan) and the final report and subsequent guidelines were entirely in terms of agency theory and shareholder supremacy: essentially, poison pills were legitimate provided they were means of getting the shareholders a better price from the predator, never if they were simply a function of the self-interest of incumbent management. The possibility that the interest of incumbent management might be in the welfare of the people they have worked with all their lives and not just in themselves has been explicitly ruled as irrelevant in court cases.

Give a dog the name self-interest and he becomes self-interested. One result of this "quiet shareholder revolution" is that top management increasingly feels entitled to selfenrichment if they serve their shareholders well. Over the five years 2001-2005, in Japan's biggest non-financial corporations employing some 7 million workers, average worker remuneration fell by 6% while directors' salaries and bonuses rose by 97% – their reward for raising dividends by 174%. A vastly different story from the last recovery from recession 1986-1990 when the figures were, respectively, plus 19%, 22% and 2%.

Old age under Shareholder Sovereignty

What price the argument that "we're all shareholders now", that the main beneficiaries of expanding shareholder returns are the great pension-fund-participant masses. Quite apart from the exceedingly skewed distribution of capital income, it is an illusion to believe that funded pension schemes somehow lessen the burden on the working generation when the pensioner/worker ratio gets to the threatened 1:1.5 or 1:2. If pension funds are largely invested domestically, there are two ways current production can be translated into pensioner incomes – the two ways being via pay-as-you-go state pensions which tax workers to pay pensioners, or through returns to market investment. The former alternative is (a) less likely to lead to poverty or the relief of poverty through grudging charity, (b) leaves current workers with exactly the same real disposable income because the capital share would have to become much larger if pension funds are to deliver, which (c) given the likely supply and demand for capital, implies a division of national income which is highly improbable.

Stakeholder power

To go back to Japan's "quasi-community model" which relates closely to what is generally known in the corporate governance literature as stakeholder theory. (Not, in fact a theory, but a prescription.) The quasi-community model, in which managers saw themselves as elders of an employee community (themselves employees of "the firm") rather than as fiduciary agents of the owners, and in which they consulted regularly on major executive decisions, with an enterprise union, with major bank creditors and even with collective *kyôryoku-kai* organisations of sub-contractors, approximated closely to most notions of the "stakeholder firm". It did, however, give too great a weight to the enterprise union and its leadership. (Union complicity in cover-ups, e.g., Minamata, being one fact one could cite for that view.)

But still, why did those unions, the major beneficiaries of the quasi-community model not defend it against the shareholder revolution? The near-zero response of the major union federation *Rengô* to all the corporate governance reforms is surprising. It can be explained in terms of (1) the usual factors accounting for the decline in union militancy and union power in advanced industrial society, plus (2) cumulative effects of educational selection on the quality of union leadership, (3) the institutional incorporation of enterprise union leadership into managerial career development tracks and

(4) the ideological dominance of the "reform = acceptance of global standards in the interests of national competitiveness" rhetoric so firmly established already by previous governments even before Koizumi made it his trademark.

Is rethink beginning?

Enron and World Com took some wind from the sails of the neo-liberal reformers marching under the "Global Standards" banner. Four years later, 2005 brought the Livedoor shenanigans – a takeover bid for a radio station by a net portal operator which ended in what looked like a traditional greenmail operation. It attracted enormous publicity because of Livedoor's CEO, a brash young arbitrageur, author of booster books for day traders and proud owner of the ambition to head the company with the world's largest market cap. His subsequent arrest for fraud and the total collapse of his company's share bubble attracted equal publicity. Ditto for the other up-and-coming arbitrageur, Murakami, already mentioned as ruined by charges of insider trading. The country was never more ripe for a wave of scepticism about the shareholder-sovereignty changes of the last decade.

But all the older generation of "nostalgics" for "the Japanese management system" could come up with was the mantra CSR, the corporate social responsibility movement which took off in Japan post-Enron. This is a very American import, whether based on the genuine moral feelings of tycoons as they wake up in the middle of the night on their yachts or their ranches and wonder what they are doing to the world, or equally Anglo-Saxon theories of "reputation resource management" as a profit-maximizing strategy. Its theoretical basis is "enlightened shareholder value theory" which holds, and sometimes tries with empirical data to prove, that you can only maximise shareholder value (in the medium to long term in which few shareholders are interested) if you care for (or appear to care for) your customers, your employees, your distributors, your suppliers, etc. Socially Responsible Investment funds which invest only in firms with good reputations exist in Japan, but with minute shares of the market. But the crucial thing is that the proponents of CSR never question the basic principle of shareholder sovereignty. They have only one answer to "Whose company is it?" "The owners', of course".

The possible shape of a stakeholder company system

The law must give a different answer to that question if there is to be a revival of the genuine concern for other stakeholders which was an essential part of Japanese management before 1990 – when managers could concentrate on managing because they were secure in their jobs, protected from takeovers by cross-shareholdings etc. *Sutêkuhorudâ* has become a common Japanese word. Successive *Keidan-ren* Chairmen, Okuda from Toyota and Mitarai from Canon, are renowned for their enlightened speeches about the need for managers to consider the interests of all stakeholders, not just shareholders.

But do they advocate institutional measures to give managers an incentive to do just that and wean them off their currently growing obsession with dividends and share-buy-backs as a means of keeping up their share price? No.

And yet, Japan still has the corporate social infrastructure for genuine stakeholder firms. In two respects: Top managers are nearly all home-grown (as they were in the America of Galbraith's *Modern Industrial State*) product of a lifetime commitment to their firm: an executive labour market hardly exists. Secondly, the bureaucratic internal promotion system has been only slightly modified by recent "merit/performance not seniority" doctrines and still is a powerful means of ensuring "commitment".

I can think of three possible institutional changes which could build on these advantages. The first is a curb on takeovers to mitigate the obsession with keeping up the share price. A Takeover Assessment Committee (TAC) could be useful. Tender bids would have to be approved by the committee before they could be launched. The interests of the consumer are already taken care of in the anti-monopoly screening provisions. The composition of the TAC would have to ensure that the effect of a possible takeover on employees, suppliers, creditors and local communities, as well as returns to shareholders were all put into the balance. It would have to work out its own guidelines, which would have to involve judgements about both the efficiency and the motives of both incumbent and would-be-new management.

The second is to make a legal requirement of something like the management-union consultation committees within firms (which are conventionally established without any legal basis, continue to exist, but play a gradually diminishing role). But they should lose their binary "top management/subordinate unionised employees" nature. Call them Enterprise Parliaments. Let them include representatives not only of the union, but also of the middle managers who have graduated beyond union membership, and are a crucial resource for expert and committed assessment of the performance of older managers. Possibly also include suppliers and major creditors.

The third is a legal requirement to produce Value Added Accounts, showing the sum total of value creation by the people working directly in the firm with the capital resources that are made available to them. The accounts should also make clear the division of value added as between employee remuneration, taxes, interest, dividends and earnings retained within the firm. The point is to make clear the "who gets what" of the firm's operations, and more particularly who gets what share of year-to-year increments in value added.

There is no denying that the younger generation is more "individualistic". They are more likely to want to work in order to live rather than live in order to work, more likely to find the conformist atmosphere of the traditional quasi-community firm so stifling that they prefer constant job-hopping to lifetime commitment. But even they might be happy to work in a genuinely stakeholder firm. And as for the older generation of business leaders who make such eloquent speeches about the Stakeholder Firm, there is only one thing to be said: Walk the talk.

ZUSAMMENFASSUNG

Der Artikel beschäftigt sich mit den jüngsten Entwicklungen rund um die corporate governance *in Japan. Die gegenwärtige japanische Diskussion dreht sich um zwei Hauptfragen: Einerseits steht der Wunsch nach Anpassung an globale, d.h. amerikanische, Standards dem Wunsch nach Beibehaltung wertvoller japanischer Traditionen gegenüber. Andererseits besteht bei der Rechtsetzung ein Spannungsverhältnis zwischen den Interessen der Eigentümer und den Arbeitnehmerrechten. Hinsichtlich des ersten Problemkomplexes haben Enron und World Com zu einer teilweisen Abkehr von Amerikanisierungstendenzen geführt. Im zweiten Problembereich schreitet der institutionelle und ideologische Wandel jedoch fort. Es ist nicht übertrieben, von einer stillen Revolution der Anteilseigner in Japan zu sprechen. Des weiteren diskutiert der Autor das Verhältnis von globalen Standards und der sozialen Infrastruktur von Corporate Governance, die jüngsten Reformen in Japan und ihre Hintergründe, die Macht der Anteilseigner und die Macht der* stakeholders. *Der Artikel schließt mit einigen konkreten Vorschlägen zur möglichen Gestaltung eines Unternehmenssystems, das die Interessen der* stakeholders *berücksichtigt, und den dafür notwendigen institutionellen Änderungen, wie etwa der Reduzierung von Übernahmen, der rechtlichen Verpflichtung zur Einsetzung von Ausschüssen unter Beteiligung von Management und Gewerkschaften sowie der rechtlichen Verpflichtung zur Erstellung von Wertschöpfungsdarstellungen.*

(Zusammenfassung durch d. Red.)