

# Seminar “Moving from Concept to Reality in Governance Reform - The Roles of Independent Directors and their Contribution to the Enhancement of Corporate Value”

(November 22, 2018)

What should you expect from independent directors<sup>1</sup> who are certified public accountants?

On November 22, 2018, a seminar entitled, “Moving from Concept to Reality in Governance Reform - The Role of Independent Directors and their Contribution to the Enhancement of Corporate Value” was held at the Japanese Institute of Certified Public Accountants (JICPA). Particularly in the latter half of the seminar, there was an enthusiastic panel discussion moderated by a JICPA member. The seminar was attended by a total of approximately 500 managers, investors, and independent directors which included those who viewed via a live feed.

The purpose of this seminar was to discuss the new Corporate Governance Code which was revised in June of this year, (June 2018). The Corporate Governance Code was first formulated in 2015 in order to improve the rate of return on equity (ROE) of Japanese corporations. The focus of the code was to encourage Japanese corporations to pay closer attention to their governance practices, institutional designs, and diversity, by employing the use of independent directors and increasing the amount of information required to be disclosed. In view of this reform, we are faced with a question - how can we utilize these improved corporate governance to enhance corporate value?

## Snapshot of the Seminar

In the first half of the seminar, two keynote speeches were given by Mr. Tsuguoki Fujinuma, a chairman of the CPAs Independent Directors and *Kansayaku*<sup>2</sup> Network with extensive experience serving as an independent director and Mr. Naoki Izumiya, the Chairman of Asahi Group Holdings who pioneered the corporate governance reform of Asahi Group Holdings.



*Mr. Fujinuma*

In Mr. Fujinuma’s presentation, he discussed how governance has changed over the course of the past 10 years, based on his first hand accumulation of knowledge and experience as an independent director as someone with a CPA qualification. Moreover, he argued on the issues where further reforms may be necessary to achieve effective governance.

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<sup>1</sup> Independent director: The listing rules of securities exchanges provide that the outside directors, as defined in the Companies Act, are independent directors where they satisfy independence criteria of securities exchanges and the company determines that they do not have the possibility of conflicts of interest with its shareholders. (Japan’s Corporate Governance Code, Tokyo Stock Exchange, Inc.)

<sup>2</sup> Companies may choose one of three main forms of organizational structure under the Companies Act (Revised in 2014): Company with *Kansayaku* Board, Company with Three Committees (Nomination, Audit and Remuneration), or Company with Supervisory Committee. A Company with *Kansayaku* Board is a system unique to Japan in which certain governance functions are assumed by the board, *kansayaku* and the *kansayaku* board. Under this system, *kansayaku* audit the performance of duties by directors and the management and have investigation power by law. (Japan’s Corporate Governance Code, Tokyo Stock Exchange, Inc.)

Mr. Izumiya then made a presentation entitled, “The Beginning of the Third Act of Governance Reform” where he emphasized the point raised earlier on improving the capacity of directors and the role of the chairman of the Board of Directors.

Mr. Izumiya mentioned the management must discuss how we are expected to effectively utilize, supervise and monitor the Board of Directors in order to maximize their effectiveness. According to Mr. Izumiya, currently, these efforts are being implemented on a trial and error basis at Asahi Group Holdings, but have yet to be clearly defined in any definitive manner. In addition, he stated that there needs to be a concerted effort made to clearly separate the roles and duties of the management team with those of the Board of Directors.



*Mr. Izumiya*

Corporations and their management teams need to clearly determine how they proceed with medium and long-term corporate management policies, assess whether their basic philosophies are being followed, have transparency with regards to their internal election processes, and address the CEO dismissal process to ensure fairness in the process. Demonstrating objectivity in these areas is not only of practical concern but, will also strengthen corporate governance by improving its effectiveness.

Furthermore, Mr. Izumiya, as an independent director, referred to a four set of items that he always keeps with him, namely:

- ① Notice of Convocation of Ordinary General Meeting of Shareholders,
- ② Integrated Report,
- ③ Securities Report,
- ④ Personal notebook

In his personal notebook, Mr. Izumiya details the company overview, current managerial issues, all pertinent figures, recent news related to the corporation, upcoming tasks, keywords and his own opinions on the agenda of the current Board of Directors. Mr. Izumiya’s insights and clarity regarding the role and obligations of independent directors was very impressive. Mr. Izumiya also stated that independent directors should express their opinions to the management without hesitation. Mr. Izumiya went on to say that independent directors with CPA qualification can specifically support management teams by providing a different perspective with regards to TOB, management integration, proposals of MBOs with clear understanding of the expectations of independent directors in the event of corporate scandals as the profession is tasked primarily as gatekeepers of capital markets. Mr. Izumiya also mentioned that he felt compelled to contribute to the development of the Japanese market by further participating in keynote speeches.

In the latter half of the seminar, there was a lively panel discussion on a diverse number of governance related issues, including the current state of governance reform, the realities of governance practices, debate on what constitutes offensive governance, in what way we can improve the effectiveness of governance reform as it pertains to the diversity of directors, the necessity and challenges of dialogue between management and investors and the expected contributions from independent directors ,particularly the expectations to CPAs to contribute to the enhancement of corporate governance.

Mr. George Iguchi from Nissay Asset Management Co., Ltd. talked on behalf of investors. Historically, the homogeneity of Japanese boards, whose main constituents are from within the



Mr. Iguchi

corporation has been considered to be one of the reasons for the lower rate of return on equity (ROE) of Japanese corporations. However, one of the remedies to this is to engage active participation of independent directors which will lead to an improvement in managerial strategy, which in turn resulting in improved ROE as a consequence of “offensive governance”. With regards to the qualifications of independent directors, it was also stated that the candidates with a basic knowledge of finance should be sufficient. More importantly, if the independent directors are those with CPA qualifications, they should be prepared to speak up to executives with the same amount of rigor they use when applying ethics.

Ms. Masako Egawa, a professor at Hitotsubashi graduate school also stated, based on her own experience as an independent director, that it is important for board directors to be independent and have the ability to resign from these positions, at any time. Furthermore, Ms. Egawa emphasized that it is important for independent director to be independent, well informed about the industry, have a well-balanced manner, and have a sound trusting relationship with the management team in order to effectively assist in corporate governance, both “defensive governance” and “offensive governance” as well as monitoring.



Ms. Egawa

Mr. Izumiya added his hopes that the most qualified candidates would be selected as independent directors, but that he hopes those candidates would be CPAs.



Mr. Uchiyama

The moderator, Mr. Hideyo Uchiyama, an administrator of the CPAs Independent Directors and *Kansayaku* Network, expanded on a number of remarks from the panelists which further developed to a breadth of discussions. Mr. Uchiyama summarized the discussion by noting that CPAs should realize that they are an important group of experts who play an integral part in improving governance of Japanese corporations, especially as it pertains to matters of future expectations. In conclusion, Mr. Uchiyama stated that CPAs should continuously improve their understanding of the markets and matters arising so as to be able to continue engaging in dialogue with management.

## Comments

Presently, the state of Japan’s corporate governance reforms are still underway. In order to continue improving corporate governance, all of the players should continue actively engaging in a dialogue in order to achieve further corporate value. This is, in and of itself, the fundamental key to success of governance reforms and the growth of corporations in Japan. The goal should be to encourage CPAs with integrity and independence, to serve as independent directors and play a critical role in creating a bright future for Japan’s corporations.

CPAs Independent Directors and *Kansayaku* Network