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The Logic and Limits of Stewardship Codes: The Case of Japan

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The Logic and Limits of Stewardship Codes: The Case of Japan

Gen Goto*

ABSTRACT

A stewardship code is a set of principles on how institutional investors should act as shareholders of companies in which they invest. Since the first was adopted by the Financial Reporting Council of the United Kingdom in July 2010, a significant number of countries, including Japan, have followed the lead of the United Kingdom in adopting their own stewardship codes. Although the contents of these codes are not identical, they generally are non-mandatory “comply or explain” rules urging institutional investors to engage more actively with their investee companies by exercising their rights as shareholders.

One might find the trend of jurisdictions adopting stewardship codes unsurprising considering the global increase in the ownership stake held by institutional investors in listed companies, and the growing expectation that these investors will play a role in the corporate governance of investee companies. However, if the goal of adopting stewardship codes is to promote better corporate governance in investee companies, then this uniform approach is rather puzzling since it is widely acknowledged that different countries have different share-ownership structures and often face different corporate governance challenges. It may well be the case that the true intention behind adopting a stewardship code could be highly contextual and, contingent on jurisdiction-specific factor.

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From such viewpoint, this article investigates the true intention behind the adoption of stewardship codes in the United Kingdom and Japan by analyzing not only the text of their principles and guidance, but also the contexts in which they were adopted. The main finding is that there is a divergence between the basic goals and orientation of the Japanese and the UK Stewardship Codes that has been largely overlooked in the literature. Although the term “stewardship” suggests that stewardship codes are premised on the logic of fiduciary duties, which compels a fiduciary to forsake its own self-interest and act in the interest of its beneficiary, the goal of the UK Stewardship Code is different. It aims to restrain excessive risk-taking and short-termism by making institutional investors more responsible to the public. In contrast, the Japanese Stewardship Code aims to change the attitude of domestic institutional investors in order to orient Japanese corporate governance towards the interests of shareholders rather than stakeholders. This goal of the Japanese Code is more compatible with the logic of stewardship than that of the UK Code. At the same time, the Japanese Government considers this goal to be in the public interest of Japan.

Another finding of this article is that different stewardship codes have different goals and that this must be taken into consideration when assessing their effectiveness. The success of the Japanese Stewardship Code will primarily depend on how well domestic institutional investors are incentivized to act in the interest of their ultimate beneficiaries and to monitor entrenched management. Conversely, the success of the UK Stewardship Code will likely depend on the extent it can prompt institutional investors to consider the interest of the public and stakeholders other than shareholders. Regulatory interventions might be necessary in both cases, but for different reasons.

I. INTRODUCTION: STEWARDSHIP CODES AND THE LOGIC OF “STEWARDSHIP”

A. Stewardship Codes as a Global Trend

A stewardship code is a set of principles on how institutional investors should act as shareholders of companies in which they invest. Since the first was adopted by the Financial Reporting Council of the United Kingdom in July 2010,¹ a significant number of countries, including Japan,² have followed the lead of the United Kingdom in adopting their own stewardship codes.³ Similar

¹ The UK Stewardship Code was originally adopted in July 2010 and later revised in November 2012 (*hereinafter*, “the 2010 UK Code” and “the 2012 Revised UK Code”). Both the original 2010 UK Code (FINANCIAL REPORTING COUNCIL, THE UK STEWARDSHIP CODE (July 2010)) and the 2012 Revised UK Code (FINANCIAL REPORTING COUNCIL, THE UK STEWARDSHIP CODE (September 2012)) are available at <https://www.frc.org.uk/investors/uk-stewardship-code/origins-of-the-uk-stewardship-code>. All websites cited in this article are last visited on October 19, 2018.

² The Japanese Stewardship Code was originally adopted in February 2014 and later revised in May 2017 (*hereinafter*, “the 2014 Japanese Code” and “the 2017 Revised Japanese Code”). The original 2014 Japanese Code (THE COUNCIL OF EXPERTS CONCERNING THE JAPANESE VERSION OF THE STEWARDSHIP CODE, PRINCIPLES FOR RESPONSIBLE INSTITUTIONAL INVESTORS (JAPAN’S STEWARDSHIP CODE): TO PROMOTE SUSTAINABLE GROWTH OF COMPANIES THROUGH INVESTMENT AND DIALOGUE (February 26, 2014)) is available at <http://www.fsa.go.jp/en/refer/councils/stewardship/20140407.html>, and its Japanese version is available at <http://www.fsa.go.jp/news/25/singi/20140227-2/04.pdf>. The 2017 Revised Japanese Code (the Council of Experts on the Stewardship Code, Principles for Responsible Institutional Investors (Japan’s Stewardship Code): To Promote Sustainable Growth of Companies through Investment and Dialogue (May 29, 2017)) is available at <http://www.fsa.go.jp/en/refer/councils/stewardship/20170529.html> and its Japanese version is available at <http://www.fsa.go.jp/news/29/singi/20170529/01.pdf>.

³ Stewardship codes around the world can be classified into three groups: those adopted by or under auspices of relevant state authorities, those adopted by stock exchanges and industrial organization of finance companies, and those adopted by private groups of institutional investors. Jennifer G. Hill, *Good Activist/Bad Activist: The Rise of International Stewardship Codes*, ECGI Law Working Paper No. 368/2017 (2017), at page 11-15 (available at <http://ssrn.com/abstract=3036357>). Among others, the first group includes stewardship codes of the United Kingdom (2010), Japan (2014), Malaysia (2014), Hong Kong (2016), and Taiwan (2016), the second group includes those of South Africa (2011), Singapore (2016) and South Korea (2016), and the third group includes those of Canada (2010), the Netherlands (2011), Switzerland (2013), International Corporate Governance Network (2016), and the United States of America (2017). Some of the stewardship codes in the second group, for example that of Singapore, could be classified in the first group if state authorities were the actual driving force behind the scene. Hill, *supra* at page 12 note 75.

The author believes that this classification is valuable and essential as it is natural to think that the authorities adopting stewardship codes have some policy objectives, which private

measures have also been taken by intergovernmental organizations, such as the Organization for Economic Co-operation and Development (OECD) and the European Union, to promote the concept of stewardship across jurisdictions.⁴ Although the contents of these codes are not identical, they generally are non-mandatory “comply or explain” approach rules urging institutional investors to engage more actively with their investee companies by exercising their rights as shareholders.

One might find the trend of jurisdictions adopting stewardship codes unsurprising when considering the global increase in the ownership stake held by institutional investors in listed companies and the growing expectation that these investors will play a role in the corporate governance of investee companies.⁵ However, if the goal of adopting stewardship codes is to promote better corporate governance in investee companies, then this uniform approach is rather puzzling.

It is widely acknowledged that different countries have different share-ownership structures and thus often face different corporate governance challenges.⁶ From such viewpoint, the assertion of two UK law professors that the transplantation of UK-Style stewardship codes “is

groups of investors may not necessarily share. In contrast, Professors Fenwick and Vermeulen, who also introduce a similar classification, do not seem to recognize the possible divergence of the goals of state authorities and private groups of investors as they simply compare “which approach is the best option”. See Mark Fenwick & Erik P. M. Vermeulen, *Institutional Investor Engagement: How to Create a ‘Stewardship Culture’*, TILEC Discussion Paper DP 2018-006 (2018), at page 37-38 and page 43 (available at <http://ssrn.com/abstract=3098235>).

⁴ See, G20/OECD Principles of Corporate Governance (September 2015), Part III (available at <https://www.oecd.org/daf/ca/Corporate-Governance-Principles-ENG.pdf>) and Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement, Chapter Ib (as amended).

⁵ See for example, G20/OECD Principles of Corporate Governance (September 2015), *supra* note 4 at 31, and Lucian A. Bebchuk, Alma Cohen & Scott Hirst, *The Agency Problems of Institutional Investors*, 31 JOURNAL OF ECONOMIC PERSPECTIVES 89, 91-93 (2017). For earlier studies, see for example, Bernard S. Black & John C. Coffee, Jr., *Hail Britannia?: Institutional Investor Behavior under Limited Regulation*, 92 MICHIGAN LAW REVIEW 1997 (1994).

⁶ REINIER KRAAKMAN ET AL., *THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH*, 3rd ed. (Oxford University Press, 2017), at 46. Other factors, such as legal systems, social institutions and culture, may also produce difference of corporate governance issues. While this is an interesting subject of research, it is beyond the scope of this article.

likely to be driven by the common concerns shared by many jurisdictions” is rather surprising,⁷ as it may well be the case that the true intention behind adopting a stewardship code in a jurisdiction could be highly contextual and contingent on jurisdiction-specific factors. Indeed, as explained in this article, this is the case in Japan.

B. The Logic of “Stewardship”

Another question arises from the term “stewardship”.

A “steward” means a “person employed to manage another’s property, especially a large house or estate” or a “person whose responsibility it is to take care of something”.⁸ In its original historical context, a “steward” was an “officer of the royal household, especially an administrator of Crown estates” in Britain.⁹ Without delving much into the British history, it would not be wrong to think of stewards in those days as being responsible to and required to demonstrate loyalty to the British royal household, whose estate is entrusted to the stewards.

In the context of modern investment, institutional investors, such as mutual funds, pension funds, insurance companies, and investment advisors, are considered to be “stewards”, as they are entrusted with their clients’ money for investment purposes. The use of the term “stewardship” suggests that stewardship codes are based on the following logic produced by an analogy with the historical “steward”: Institutional investors must be loyal to their clients, who have entrusted their money to the institutions for investment purposes, and should exercise their rights as shareholders of investee companies in order to fulfill their responsibility as “stewards” of their clients.¹⁰

⁷ Iris H.-Y. Chiu & Dionysia Katelouzou, *From Shareholder Stewardship to Shareholder Duties: Is the Time Ripe?* in Hanne S. Birkmose (ed.), *SHAREHOLDERS’ DUTIES* (Wolters Kluwer, 2017) at 131, 135. See also *ibid.* at 133 (arguing that duty of institutional investors regarding stewardship/engagement “is relevant to different European jurisdictions despite any differences in the ownership structures”).

⁸ The Oxford Dictionary (online version) <https://en.oxforddictionaries.com/definition/steward>.

⁹ *Ibid.*

¹⁰ Those who are familiar with the UK Stewardship Code might argue that the logic of stewardship stipulated in the text above does not fit the UK Code, which considers institutional investors rather as stewards of investee companies. The author agrees. Indeed, the point of this article is to show that such framing of a stewardship code is UK-specific (or Europe-specific) and is not necessarily universally shared - at least not by the Japanese Stewardship Code. See *infra*, Part I, Section C and Part III, Section C.

One would notice that this logic of “stewardship” is essentially that of fiduciary duties, which compels a fiduciary to forsake its own self-interest and act only in the interest of its beneficiary.¹¹ Indeed, some of the relationships between institutional investors and their clients can be described as a fiduciary relationship. For example, an investment advisor hired by a public pension fund to manage a part of its fund is a fiduciary to the pension fund.¹² By avoiding the use of the term “fiduciary”, which is a well-established legal term in the common-law world with a defined scope,¹³ stewardship codes have expanded the range of actors they cover, especially those that would not necessarily be considered fiduciaries.¹⁴

While the above logic of stewardship focuses on the interest of ultimate beneficiaries,

¹¹ See for example, Hiroyuki Kansaku, *Koporeto gabanansu kojyo ni muketa naigai no doko – Suchuwadoshippu kodo wo chushin toshite* [Developments towards the Improvement of Corporate Governance in Japan and Other Countries: With Focus on Stewardship Codes], 2030 SHOJHOMU 11, at 13 (2014).

¹² For example, OECD Principles recommends, without using the term “stewardship”, that “institutional investors acting in a fiduciary capacity should disclose their corporate governance and voting policies with respect to their investments”.

¹³ For example, the investment advisor in the example above is not in a direct relationship with ultimate beneficiaries of the pension fund and thus may not be considered as a fiduciary in relation to the ultimate beneficiaries. Also, the relationship between a life insurance company and its policyholders is generally considered as that of a contract and not of a fiduciary, although insurance company invests the money paid by the policyholders as premiums out of which insurance proceeds will be paid. The same would apply to the relationship between a proxy advisor and its clients (and their ultimate beneficiaries). See Iris H.-Y. Chiu & Dionysia Katelouzou, *Making a Case for Regulating Institutional Shareholders’ Corporate Governance Roles*, 2018 JOURNAL OF BUSINESS LAW 67, at 79-81.

¹⁴ See Hiroyuki Kansaku, *Nihon-ban suchuwadoshippu kodo no kihansei ni tsuite* [On the Nature of the Japanese Stewardship Code as a Norm], in Etsuro Kuronuma & Tomotaka Fujita (eds.), *KIGYOHO NO SHINRO – EGASHIRA KENJIRO SENSEI KOKI KINEN* [Future Courses of Enterprise Law - In Celebration of the 70th Birthday of Professor Kenjiro Egashira] (Yuhikaku, 2017), 1005, at page 1014. Of course, the binding power of stewardship codes taking the “comply or explain” approach is not as strong as that of fiduciary duties imposed by law.

Interestingly, the Financial Services Agency of Japan rather turned to the term “fiduciary duty”, which is an imported concept for Japan that does not share the common-law tradition, as a means to change the behavior of sellers of financial instruments, such as banks selling mutual fund or variable life insurance, to disclose more information to their customers. See Nobuko Matsumoto, *Kinyu bunya ni okeru “fidyushari=dyuthi no yogoho ni tsuite no ichi kosatsu* [A Study on the Terminology of “Fiduciary Duty” in Financial Regulation], in Yoshihisa Nomi, Norio Higuchi & Hideki Kanda (eds.), *SHINTAKU HOSEI NO SHIN JIDAI: SHINTAKU NO GENDAITEKI TENKAI TO SHORAI TENBOU* [The New Era of Trust Law: Modern Developments and Future Prospects of Trusts] (Kobundo, 2017) at 223.

scholarly debate on the role of institutional investors mentioned in the previous section focuses on improving corporate governance of investee companies.¹⁵ This difference in focus raises a possibility that stewardship codes are not necessarily based on the logic of stewardship, but rather focus on corporate governance of investee companies.

C. The Japanese Code and the UK Code: Are they the same?

Are stewardship codes about the interests of ultimate beneficiaries, or are they about corporate governance of investee companies? Interestingly, there is an important difference between the Japanese Stewardship Code and the UK Stewardship Code on this point.

The preface of the Japanese Stewardship Code begins with the following definition of “stewardship responsibilities”:

In this Code, “stewardship responsibilities” refers to the responsibilities of institutional investors to enhance the medium- to long-term investment return for their clients and beneficiaries (including ultimate beneficiaries; the same shall apply hereafter) by improving and fostering the investee companies’ corporate value and sustainable growth through constructive engagement, or purposeful dialogue, based on in-depth knowledge of the companies and their business environment.¹⁶

In contrast, the preface of the current UK Stewardship Code as revised in 2012 states the aim of stewardship in its first paragraph as follows:

Stewardship aims to promote the long term success of companies in such a way that the ultimate providers of capital also prosper. Effective stewardship benefits companies, investors and the economy as a whole.¹⁷

¹⁵ In contrast, the question raised in Part I, Section A that countries facing different issues are somehow adopting a common measure would not be a problem here as the relationship between ultimate beneficiaries and fund managers may not be so different among countries.

¹⁶ The 2014 Japanese Code, *supra* note 2 at page 1. The definition of stewardship responsibilities remains unchanged in the 2017 Revised Japanese Code, *supra* note 2 at page 3.

¹⁷ The 2012 Revised UK Code, *supra* note 1 at page 1.

These codes are ostensibly alike as they use similar wording on the same two issues. The first is the interest of ultimate beneficiaries (“the medium- to long-term investment return for their clients and beneficiaries” (Japan) or the prosperity of “the ultimate providers of capital” (UK)). The second is the growth of investee companies (“improving and fostering the investee companies’ corporate value and sustainable growth” (Japan) or “the long-term success of companies” (UK)).

The two codes, however, are structured differently and thus seem to emphasize different points. By using the prepositions “to” and “by”, the Japanese Code seems to prioritize the enhancement of “the medium- to long-term investment return for [institutional investors’] clients and beneficiaries” as the goal of stewardship responsibility and consider sustainable growth of investee companies as a means to achieve this goal.¹⁸ In contrast, the UK 2012 Code seems to put emphasis on “the long-term success of [investee] companies”, which is brought first, and to subordinate the interest of ultimate providers of capital by using the words “in such a way” and “also”. Somewhat ironically, Japan seems to demonstrate greater fidelity to the logic of “stewardship”, as set out earlier, than the United Kingdom, the motherland of stewardship codes.

D. Research questions

From this divergence, which has been largely overlooked in the literature,¹⁹ a few questions arise. What is, or are, the intended goal(s) of stewardship codes? Why are countries pursuing different goals and trying to use the same measure to achieve them? How compatible are these goals with the logic of stewardship and can they be achieved by adopting stewardship codes?

¹⁸ In response to one of the comments received in the public comment procedure criticizing the inclusion of sustainable growth of investee companies in the scope of stewardship responsibility, the Council of Experts Concerning the Japanese Version of the Stewardship Code admitted that the final goal of institutional investors is to enhance the medium- to long-term investment return for their clients and beneficiaries, while asserting that it is important to improve and foster the investee companies’ corporate value and sustainable growth through constructive engagement. See THE COUNCIL OF EXPERTS CONCERNING THE JAPANESE VERSION OF THE STEWARDSHIP CODE, *Wabun ni taisuru komento no gaiyo oyobi kentokai no kangaekata* [The Summary of the Comments to the Japanese Version of the Draft and the Council’s View on Them] (April 22, 2014, available at <http://www.fsa.go.jp/news/25/singi/20140422-2/01.pdf>), Comment No.2 at page 1.

¹⁹ See *infra* note 152-158 and accompanying text.

This Article addresses these questions by drawing on the Japanese experience and by comparing it with the United Kingdom. Briefly stated, there is a divergence between the basic goals and orientation of the Japanese and the UK Stewardship Codes. Although the term “stewardship” suggests that stewardship codes are based on the logic of a fiduciary duty that compels a fiduciary to forsake its own self-interest and act in the interests of its beneficiary, the goal of the UK Stewardship Code is instead to restrain excessive risk-taking and short-termism by making institutional investors more responsible to the public. In contrast, the Japanese Stewardship Code aims to change the attitude of domestic institutional investors so as to make Japanese corporate governance more oriented towards the interests of shareholders rather than stakeholders.

The remainder of this Article starts with a deeper look at the background and the contents of the UK Stewardship Code with a view to identify its intended goal (Part II). After a similar exercise with the Japanese Stewardship Code (Part III), this Article analyzes whether the intended goals of the UK and Japanese codes are compatible with the logic of stewardship, and whether these codes can achieve their respective goals (Part IV).

II. THE ORIGIN OF STEWARDSHIP CODES: THE CASE OF THE UNITED KINGDOM

A. Inconsistency within the 2012 UK Code

As discussed above, the preface to the current 2012 revised version of the UK Stewardship Code, lists two goals of stewardship: (1) “the long term success of companies”; and, (2) the prosperity of “the ultimate providers of capital”. However, the first goal appears to have priority over the second. Such a focus on the long-term success of investee companies is also reflected in the second paragraph of the preface, which states that “responsibility for stewardship is shared” in publicly listed companies; that “the primary responsibility rests with the board of the company”; and that investors “also play an important role in holding the board to account for the fulfilment of its responsibilities”.²⁰ If, however, one takes the logic of stewardship discussed in Part I, Section B seriously, it should be institutional investors that bear the primary responsibility to their clients and ultimate beneficiaries.

In contrast, the principles of the 2012 Revised UK Stewardship Code, which are

²⁰ The 2012 Revised Code, *supra* note 1 at page 1.

described as “the core of the Code”,²¹ are stipulated in the following manner:

So as to protect and enhance the value that accrues to the ultimate beneficiary, institutional investors should:

- 1. publicly disclose their policy on how they will discharge their stewardship responsibilities.*
- 2. have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed.*
- 3. monitor their investee companies.*
- 4. establish clear guidelines on when and how they will escalate their stewardship activities.*
- 5. be willing to act collectively with other investors where appropriate.*
- 6. have a clear policy on voting and disclosure of voting activity.*
- 7. report periodically on their stewardship and voting activities.*²²

Clearly, the chapeau of these seven principles, which was added by the 2012 revision, emphasizes the interests of ultimate beneficiaries as the goal. It does not even refer to the interest of investee companies. There is thus a clear inconsistency between the preface and the principles of the 2012 Revised UK Stewardship Code on which aspect to emphasize, the interest of investee companies or that of ultimate beneficiaries. Unsurprisingly, the UK Stewardship Code has been criticized as “unclear as to whom shareholders are accountable to”.²³ To understand the origin of this inconsistency, the following section will examine the background of the UK Stewardship Code.

²¹ The 2012 Revised Code, *supra* note 1 at page 4. Each principle is accompanied by detailed guidance. *Ibid.* at page 6-10.

²² The 2012 Revised UK Code, *supra* note 1 at page 5.

²³ Arad Reisberg, *The UK Stewardship Code: On the Road to Nowhere?* 15 JOURNAL OF CORPORATE LAW STUDIES 217, 229 (2015). Similar views are expressed by Chiu & Katelouzou, *supra* note 13 at 87 and Paul Davies, *Shareholders in the United Kingdom*, in Jennifer G. Hill & Randall S. Thomas (eds.), RESEARCH HANDBOOK ON SHAREHOLDER POWER (Edward Elgar, 2015) 355, at 373.

B. The Background of the UK Stewardship Code

1. The Walker Review

In November 2009, in the aftermath of the global financial crisis in the preceding years, Sir David Walker submitted a report known as the “Walker Review”²⁴ commissioned by the UK government. The task, as described by the UK government, was “to review corporate governance in UK banks in light of the experience of critical loss and failure throughout the banking system”, on the premise that “serious deficiencies in prudential oversight and financial regulation in the period before the crisis were accompanied by major governance failures within banks” and that these factors “contributed materially to excessive risk taking and to the breadth and depth of the crisis”.²⁵

In this review, Sir David recommended that the “remit of the FRC [Financial Reporting Council] should be explicitly extended to cover the development and encouragement of adherence to principles of best practice in stewardship by institutional investors and fund managers” and that the “Code on the Responsibilities of Institutional Investors, prepared by the Institutional Shareholders’ Committee, should be ratified by the FRC and become the Stewardship Code”.²⁶

The Walker Report focused on the role of institutional investors since there was “a widespread acquiescence by institutional investors and the market in the gearing up of the balance sheets of banks (and also of many other companies) as a means of boosting returns on equity”.²⁷ Such an attitude “was not necessarily irrational from the standpoint of the immediate interests of shareholders who, in the leveraged limited liability business of a bank, receive all of the potential upside whereas their downside is limited to their equity stake, however much the bank loses

²⁴ SIR DAVID WALKER, A REVIEW OF CORPORATE GOVERNANCE IN UK BANKS AND OTHER FINANCIAL INDUSTRY ENTITIES: FINAL RECOMMENDATIONS (November 26, 2009) (*hereinafter* “the Walker Review”), available at http://webarchive.nationalarchives.gov.uk/+http://www.hm-treasury.gov.uk/d/walker_review_261109.pdf. Sir David is a prominent British banker and a former officer of the UK Treasury and Bank of England. See [https://en.wikipedia.org/wiki/David_Walker_\(banker\)](https://en.wikipedia.org/wiki/David_Walker_(banker)).

²⁵ The Walker Review, *supra* note 24 at page 9.

²⁶ The Walker Review, *supra* note 24 at Recommendations 16 and 17, at page 17.

²⁷ The Walker Review, *supra* note 24 at para.5.10 at page71. See also the Walker Review, *supra* note 24 at para.1.10 at page 26.

overall in a catastrophe”.²⁸ However, “while shareholders enjoy limited liability in respect of their investee companies, in the case of major banks the taxpayer has been obliged to assume effectively unlimited liability”.²⁹ In another part, the Walker Review criticizes the “increased shareholder pressure on boards to perform in the short term” before the Financial Crisis, and regards “specific short-term initiative[s] such as increased leverage, spin-offs, acquisitions or share buybacks” as “opportunistic behavior” as they brought “a stronger stock price and higher short-term earnings” “at the expense of increased credit risk and potential erosion in credit quality to the detriment of bondholders and other creditors”.³⁰

It is in this context that the Walker Review emphasizes the importance of discharging the responsibilities of shareholders as owners, and asserts that “those who have significant rights of ownership and enjoy the very material advantage of limited liability should see these as complemented by a duty of stewardship”.³¹ The Walker Review states that this view “would be shared by the public, as well as those employees and suppliers who are less well-placed than an institutional shareholder to diversify their exposure to the management and performance risk of a limited liability company”.³²

To summarize, the goal of the Walker Review was to make institutional investors who are shareholders of public companies more responsible to the general public by monitoring the management of those companies so as to restrain excessive risk taking.³³ This goal is

²⁸ The Walker Review, *supra* note 24 at para.5.10 at page71. See also the Walker Review, *supra* note 24 at para.1.8 at page 25.

²⁹ The Walker Review, *supra* note 24 at page 12.

³⁰ The Walker Review, *supra* note 24 at para.5.27 at page 78.

³¹ The Walker Review, *supra* note 24 at page 12 and para.5.7 at page 70.

³² The Walker Review, *supra* note 24 at para.5.7 at page 70.

³³ Iris H-Y Chiu, *Institutional Shareholders as Stewards: Toward a Ne Conception of Corporate Governance*, 6 BROOKLYN JOURNAL OF FINANCIAL AND COMMERCIAL LAW 387, at 396 (2012). It may be worth noting that the Walker Review was not the first policy document to count on institutional investors’ monitoring role from the viewpoint of public interest. The Cadbury Report, which was published in 1992 in the wake of financial scandals at Maxwell Communications and Bank of Credit and Commerce International, turned to institutional investors to engage with their investee companies and to make positive use of their voting rights to achieve better corporate governance. REPORT OF THE COMMITTEE ON THE FINANCIAL ASPECTS OF CORPORATE GOVERNANCE (May 1992), para.6.9-6.12, available at <http://www.ecgi.org/codes/documents/cadbury.pdf>.

understandable given the context of the post-crisis crimate.³⁴

It is not so clear, however, how the adoption of a stewardship code would help in achieving these public interest goals. While the Walker Review describes this responsibility of shareholders as “a duty of stewardship” without clarifying to whom such a duty is owed and expects that many “ultimate beneficiaries, trustees and other end investors would no doubt wish to be supportive of” it,³⁵ the above goal would rather contradict with the logic of “stewardship” discussed in Part I, which focuses on maximizing the interests of ultimate beneficiaries of institutional investors.

2. The ISC Code

Interestingly, the Code on the Responsibilities of Institutional Investors (the ISC Code),³⁶ which was drafted by the Institutional Shareholders’ Committee (ISC) and recommended by the Walker Review to the FRC for ratification, did not share the same goal as the Walker Review. In particular, the ISC Code declares that the “duty of institutional investors is to their end-beneficiaries and/or clients and not to the wider public”.³⁷ Also, the paragraph describing the aim of the code places improving “long-term returns to shareholders” ahead of reducing “the risk of catastrophic outcomes due to bad strategic decisions” and “helping with the efficient exercise of governance responsibilities”.³⁸

As the ISC is not a governmental agency but a private organization formed by trade associations of British institutional investors,³⁹ it is quite understandable that this code places the

³⁴ Professor Reisberg describes the mood of the period as “Something had to be done quickly and, preferably, visibly”. Reisberg, *supra* note 23 at 221.

³⁵ The Walker Review, *supra* note 24 at para.5.7 at page 70 and para.5.9 at page 71.

³⁶ INSTITUTIONAL SHAREHOLDERS’ COMMITTEE, THE CODE ON THE RESPONSIBILITIES OF INSTITUTIONAL INVESTORS (November, 2009) (*hereinafter* “the ISC Code”), available at https://www.theinvestmentassociation.org/assets/components/ima_filesecurity/secure.php?f=i ndustry-guidance/isc-01.pdf. This code is also included in the Annex 8 of the Walker Review.

³⁷ ISC Code, *supra* note 36 at page 2. The declaration in the text was made after stating that the amount of resources of institutional investors should be “sufficient to allow them to fulfill their responsibilities effectively” but be “commensurate with the benefits derived”.

³⁸ ISC Code, *supra* note 36 at page 1.

³⁹ The members of the ISC as of 2009 are the Association of British Insurers, the Association of Investment Trust Companies, the National Association of Pension Funds, and the Investment Management Association. ISC Code, *supra* note 36 at page 1, footnote 1.

interests of clients and ultimate beneficiaries of institutional investors above that of the wider public. This stance, which the ISC has held since at least 2002,⁴⁰ however, has apparently been ignored by the Walker Review.⁴¹

Why did the Walker Review recommend that the FRC shall ratify the ISC Code and grant it “quasi-official imprimatur”⁴² despite fundamental differences in their orientation and philosophy? The Walker Review seems to assume that investors who engage with investee companies “are likely to be relatively long-term holders for whom divestment in potential problem situations comes to be seen as a last rather than first resort” and thus that they would focus on long-term profits and not pursue “specific short-term initiative[s] such as increased leverage, spin-offs, acquisitions or share buybacks” that were seen in the period before the Financial Crisis.⁴³ It is, however, difficult not to criticize this assumption as “naïve” given the behavior of institutional investors prior to the financial crisis.⁴⁴

⁴⁰ The statement that “(t)he duty of institutional investors is to their end-beneficiaries and/or clients and not to the wider public” appears in “the Responsibilities of Institutional Shareholders and Agents – Statement of Principles” published by the ISC in 2002 and its update in 2007 (available at http://www.ecgi.org/codes/documents/isc_statement_of_principles.pdf and https://www.plsa.co.uk/portals/0/Documents/0039_ISC_Statement_of_Principles_2007_0607.pdf). The 2002 document was the ISC’s response to a proposal of the Myners Report to impose a duty on UK-based pension funds to exercise voting rights as shareholders of investee companies on issues that may affect the value of the plan’s investment. See PAUL MYNERS, INSTITUTIONAL INVESTMENT IN THE UNITED KINGDOM: A REVIEW (March 2001) (*hereinafter* “the Myners Report”), at para.5.89-5.93 at page 92-93 (available at <http://webarchive.nationalarchives.gov.uk/20070506151732/http://www.hm-treasury.gov.uk/media/2F9/02/31.pdf>) and Brian R. Cheffins, *The Stewardship Code’s Achilles’ Heel*, 72 MODERN LAW REVIEW 1004, 1008-1009 (2010). From the perspective of this article, it is important to note that the Myners Report differs from the Walker Review in focusing on the financial self-interest of institutional investors to serve their clients rather than the governance of investee companies and does not try to make “a public interest argument about shareholder responsibility”. The Myners Report, para.5.76 at page 90. See also para.3 of the summary at page 4 (“The review does not seek to argue that the institutions whose investment behaviour it examines have some public interest responsibility to invest in certain ways.”).

⁴¹ Cf. the Walker Review, *supra* note 24 at para.5.13 at page 72.

⁴² The Walker Review, *supra* note 24 at para.5.38 at page 82-83.

⁴³ See, the Walker Review, *supra* note 24 at para.5.16 at page 73 and para.5.27-5.29 at page 78-79.

⁴⁴ Chiu & Katelouzou, *supra* note 13 at 76. See also Reisberg, *supra* note 23 at 233 (describing the attempt to incentivize engagement as “an uphill battle where long-term performance has become less relevant as investors place more value on the ability to mitigate risk and the

3. The 2010 UK Code

In any event, the Financial Reporting Council⁴⁵ followed the recommendation of the Walker Review and issued a consultation paper in January 2010 seeking public feedback on whether it should adopt the ISC Code as the UK Stewardship Code.⁴⁶

Although the FRC referred to the responsibility of institutional investors “to ensure that the asset managers act diligently and in the best interest of the ultimate owners”,⁴⁷ improved governance and performance of investee companies, more efficient operation of capital markets and increased confidence in business were stated as the first potential benefits of more effective engagement.⁴⁸ Upon the adoption of the ISC Code as the UK Stewardship Code in July 2010, the FRC replaced the introduction of the ISC Code with a new preface and deleted the declaration of the ISC Code that the “duty of institutional investors is to their end-beneficiaries and/or clients and not to the wider public”.⁴⁹ Taken together, the 2010 UK Code appears to share the same goal as the Walker Review.⁵⁰

This orientation of the 2010 UK Code is obscured, however, because the aim in the newly drafted preface is almost an exact copy of that of the ISC Code, stating that the

freedom to detach themselves from an underperforming company.”).

⁴⁵ The Financial Reporting Council is an independent regulator of the United Kingdom, the primary responsibility of which is to oversee auditors, accountants and actuaries to promote transparency and integrity in business. See <https://www.frc.org.uk/>

⁴⁶ FINANCIAL REPORTING COUNCIL, CONSULTATION ON A STEWARDSHIP CODE FOR INSTITUTIONAL INVESTORS (January 2010), available at <https://www.frc.org.uk/consultation-list/2010/consultation-on-a-stewardship-code-for-institution>.

⁴⁷ FINANCIAL REPORTING COUNCIL, *supra* note 46 at para.1.3 at page 2.

⁴⁸ FINANCIAL REPORTING COUNCIL, *supra* note 46 at para.1.11 at page 4. As other benefits, the consultation paper states as follows: “Greater clarity in the respective responsibilities of asset managers and asset owners and strengthened accountability of institutional shareholders to their clients will also strengthen trust in the financial system. A clear understanding of these responsibilities will also assist beneficial owners in setting the terms of their fund mandates and in holding asset managers accountable”.

⁴⁹ See, FINANCIAL REPORTING COUNCIL, IMPLEMENTATION OF THE UK STEWARDSHIP CODE (July 2010), at para.18 at page 4, available at <https://www.frc.org.uk/getattachment/34d58dbd-5e54-412e-9cdb-cb30f21d5074/Implementation-of-Stewardship-Code-July-2010.pdf>.

⁵⁰ Chiu, *supra* note 33 at 395, 416.

“Stewardship Code aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities”.⁵¹ The principles and guidance stated in this 2010 UK Code are also essentially the same as those of the ISC Code,⁵² as the FRC “decided to adopt the Code in its current form” “with only limited amendments” in order “to build on the momentum generated by the Walker Review, the ISC’s initiative, and the debate on engagement stimulated by the changes to the UK Corporate Governance Code and the consultation of this Code”.⁵³

4. The 2012 Revised UK Code

The FRC made it clear in 2010 that it would revise the UK Stewardship Code as necessary.⁵⁴ One of the aims of this revision, which took place in 2012, was to clarify the meaning of the term “stewardship”.⁵⁵ Consequently, the preface of the Code was substantially redrafted. As mentioned in Part I, Section C above, the 2012 Revised UK Code provides that stewardship “aims to promote the long term success of companies in such a way that the ultimate providers of capital also prosper”.⁵⁶ When comparing this statement with the aim of the 2010 Code, which is “to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities”, it is clear that the 2012 Revised Code placed more emphasis on “the long-term success of [investee] companies” as its goal over the interest of ultimate beneficiaries.

⁵¹ The 2010 UK Code, *supra* note 1 at page 1.

⁵² The formulation of the chapeau of the principles in the 2010 UK Code, which simply states “Institutional investors should”, differs from that of the 2012 Revised UK Code cited earlier. See *supra* note 22 and accompanying text.

⁵³ FINANCIAL REPORTING COUNCIL, IMPLEMENTATION OF THE UK STEWARDSHIP CODE (July 2010), para.7 and 9 at page 2. Some commentators have criticized the FRC for not taking the opportunity to strengthen the standards of the ISC Code. See Lee Roach, *The UK Stewardship Code*, 11 JOURNAL OF CORPORATE LAW STUDIES 463, 479-493.

⁵⁴ The 2010 UK Code, *supra* note 1 at page 3.

⁵⁵ FINANCIAL REPORTING COUNCIL, REVISIONS TO THE UK STEWARDSHIP CODE: CONSULTATION DOCUMENT (April 2, 2012) (available at <https://www.frc.org.uk/consultation-list/2012/consultation-document-revisions-to-the-uk-steward>), para.6 at page 1. The other aims were to clarify the respective roles and responsibilities of asset owners and managers, to address some issues identified in the initial consultation in 2010, to take into account lessons learned during the initial implementation of the Code and to update the Code to reflect developments in market practice. See *ibid.*, para.6-8 at page 1-2.

⁵⁶ The 2012 Revised UK, *supra* note 1 at para.1 at page 1.

At the same time, the 2012 Revised UK Code created the inconsistency described in Part II, Section A by emphasizing the interest of ultimate beneficiaries with the phrase “So as to protect and enhance the value to the ultimate beneficiary,” in the chapeau of “The Principles of the Code”.⁵⁷ Similar references to the interest of ultimate beneficiaries are also made in the new guidance to Principles 1 and 2.⁵⁸

Unfortunately, the reason for these amendments is not fully explained in the consultation paper for the 2012 revision. On the subject of revisions to the preface and the guidance to Principle 1, the consultation paper only refers to the existence of “some confusion in the UK market and overseas as to what ‘stewardship’ means” such as “a perception in some quarters that the Stewardship Code is solely concerned with socially responsible investment”.⁵⁹ As to the objectives provided in the chapeau of the principles, the consultation paper explains that this phrase was moved from Principle 4 of the original 2010 Code as it “relates to all the principles”,⁶⁰ but does not explain how it relates to the statement of the aim of the Stewardship Code in the new preface.

5. The Kay Review

In the author’s view, the 2012 revision of the UK Stewardship Code seems to be influenced by the position of the Kay Review,⁶¹ the first recommendation of which states that the “Stewardship

⁵⁷ No change or addition is made to the content of the seven principles itself. FINANCIAL REPORTING COUNCIL, *supra* note 55 at para.4 at page 1.

⁵⁸ The 2012 Revised UK Code, *supra* note 1 at the second paragraph of the guidance to Principle 1 (“The policy should disclose how the institutional investor applies stewardship with the aim of enhancing and protecting the value for the ultimate beneficiary or client.”) and the third paragraph of the guidance to Principle 2 (“Institutional investors should put in place, maintain and publicly disclose a policy for identifying and managing conflicts of interest with the aim of taking all reasonable steps to put the interests of their client or beneficiary first.”).

⁵⁹ FINANCIAL REPORTING COUNCIL, *supra* note 55 at para.5 at page 5.

⁶⁰ FINANCIAL REPORTING COUNCIL, *supra* note 55 at para.36 at page 11.

⁶¹ THE KAY REVIEW OF UK EQUITY MARKETS AND LONG-TERM DECISION MAKING: FINAL REPORT (July 2012) (*hereinafter* “the Kay Review: Final Report”), available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf. To be precise, the Final Report of the Kay Review was published in July 2012 and thus was unable to be taken into consideration by the consultation paper of the FRC, which was published in April of that year. However, the Interim Report of the Kay Review, which was published in February 2012 and is referred to in the consultation paper, had already expressed the views that will be discussed in the

Code should be developed to incorporate a more expansive form of stewardship, focusing on strategic issues as well as questions of corporate governance”.⁶²

This “expansive form of stewardship” is premised on the Kay Review’s “belief that the investment chain will work best if those who invest funds in equity markets have trust and confidence in the agents with which they place the funds and if the companies which list on equity markets have respect for those who rely on their earnings and cash flow to generate returns on their savings and security in their retirement”.⁶³ In other words, the Kay Review expects institutional investors to “trust” the management of investee companies upon engagement, “which is most commonly positive and supportive, and not merely critical”.⁶⁴

The aim of the Kay Review in promoting this “expansive form of stewardship” is, as

following texts. See FINANCIAL REPORTING COUNCIL, *supra* note 55 at para.4 at page 1 (referring to the view expressed in the Interim Report of the Kay Review that the 2010 Stewardship Code “should be given time to settle”) and THE KAY REVIEW OF UK EQUITY MARKETS AND LONG-TERM DECISION MAKING: INTERIM REPORT (February 2012), available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31544/12-631-kay-review-of-equity-markets-interim-report.pdf (focusing on stewardship and engagement as essential means for equity markets to achieve the ends of “allowing companies to make long term decisions appropriate to their business and ... allowing savers to make financial plans appropriate to their objectives” (at para.2.15 and 2.16 at page 8, para.2.21 at page 9 and para.2.23 at page 11); observing that asset managers concerned with stewardship “would be expected to engage with, and be committed to, the companies in which they held stock” and “normally be supportive of company management, but would be ready to engage in constructive criticism and, in the extreme cases, to act themselves or in conjunction with others to effect change” (para.2.20 at page 9); acknowledging the concern that “the time horizons adopted by savers ... to judge their asset managers was significantly shorter than the time horizon over which the saver ... was looking to maximise a return” and that this “emphasis ... on short term performance investing influenced the style of asset management in ways that could disadvantage the beneficial owner” by emphasizing “trading rather than investing” (at para.6.32 at page 36); distinguishing asset managers “whose primary focus is on the activities of the company – its business, its strategy, and its likely future earnings and cash flow – and those whose primary focus is on the market for the shares of the company – the flow of buy and sell orders, the momentum in the share price, the short term correlations between the prices of different stocks” (para.6.6 at page 31)).

⁶² The Kay Review: Final Report, *supra* note 61 at page 13.

⁶³ The Kay Review: Final Report, *supra* note 61 at para.6.4 at page 45. See also Principle 1, *ibid.* at page 12.

⁶⁴ The Kay Review: Final Report, *supra* note 61 at para.6.3 at page 44-45. It must be noted that the word “trust” may not be used consistently in the Kay Review as para.6.2 refers to the trust on institutional investors by their clients (“The honest steward expects to be rewarded for the discharge of that *trust*, but on a basis of full disclosure and only on that basis.” (emphasis added by the author)).

the official title of the Review suggests, to contribute to “good long-term decision making in British business and finance”.⁶⁵ To put it differently, the Kay Review’s emphasis on stewardship of institutional investors was directed at combating short-termism, which is defined as “a tendency to under-investment, whether in physical assets or in intangibles such as product development, employee skills and reputation with customers, and as hyperactive behaviour by executives whose corporate strategy focuses on restructuring, financial re-engineering or mergers and acquisitions at the expense of developing the fundamental operational capabilities of the business”.⁶⁶

In its foreword, the Kay Review expresses the view that such short-termism is detrimental to the competitive advantages of British companies in global markets and the prosperity of the United Kingdom.⁶⁷ Although the Kay Review also refers to the interests of British savers and pension beneficiaries “to benefit from the activity of these businesses through returns to direct and indirect ownership of shares in UK companies”,⁶⁸ its focus seems to be on the long-term profitability of UK companies rather than on the interest of UK ultimate beneficiaries.⁶⁹ Thus, the Kay Review essentially shares the goal of the Walker Review, which is

⁶⁵ The Kay Review: Final Report, *supra* note 61 at para.6.27 at page 48. The Kay Review sets out the principles relevant to good long-term decision making so as “to focus the attention of directors on the success of the company in the long-term: to lengthen the time scale of measurement of investment performance by influencing the priorities of asset holders and asset managers: to shorten the time horizon of value discovery by placing greater emphasis on the relationship between the asset manager and the company”. The Kay Review: Final Report, *supra* note 61 at para.6.28 at page 48.

⁶⁶ The Kay Review: Final Report, *supra* note 61 at para.vi at page 10. See also para.1.1 and 1.2 at page 14.

⁶⁷ The Kay Review: Final Report, *supra* note 61, Foreword at page 5 (“British business must invest and must develop its capacity for innovation, its brands and reputations, and the skills of its workforce. Only in this way can we create and sustain the competitive advantages in global markets which are necessary to maintain our prosperity.”). The Kay Review also seems to blame short-termism in the UK equity market as one of the reasons that no companies like Amazon, Apple or Google has emerged in Britain “to take the place of the financial institutions which failed in the recent crisis”. The Kay Review: Final Report, *supra* note 61 at para.1.27 at page 20.

⁶⁸ The Kay Review: Final Report, *supra* note 61 at page 9. See also the Kay Review: Final Report, *supra* note 61, Foreword at page 5 (“Through success in world markets, British companies will earn the returns on investment which are necessary to pay our pensions and enable us to achieve our long-term financial goals.”).

⁶⁹ The Kay Review emphasizes the importance of fiduciary duty and standards in investment chain, which “require that the client’s interests are put first”, but limits the type of the client’s interest to be taken into account to long-term and excludes short-term. The Kay Review:

to restrain excessive risk-taking at the cost of stakeholders other than shareholders.

6. Summary: The Goal of the UK Stewardship Code

The above analysis of the background of the UK Stewardship Code illuminates the importance of distinguishing between the UK practice of engagement by traditional institutional investors and the Stewardship Code in conjunction with the Walker and the Kay Reviews. While the UK practice has been carried out for the interest of their beneficiaries as expressed by the ISC, the UK Code and the two Reviews as policy documents focus on public interest by restraining excessive risk-taking and short-termism.⁷⁰ The reference to the interest of ultimate beneficiaries in the UK Stewardship Code, especially in the 2012 version, should be read restrictively as referring to an interest in long-term returns.

C. Academic Responses in the UK

Legal scholars in the UK generally seem to share the above orientation of the UK Stewardship Code,⁷¹ although commentators have been largely critical of the Code's ability to achieve its intended goal.

For example, after correctly recognizing that the aim of the Walker Review is to impose a duty of stewardship on shareholders who enjoy limited liability,⁷² Professor Cheffins questions the effectiveness of the Code as foreign investors who presently own more than 40% of the shares of UK listed companies today are not "under any direct onus to commit to the Code's terms".⁷³ Professor Davies also observes that "it is difficult to believe that the new regime"

Final Report, *supra* note 61, Principle 5 at page 12, para.7.9 at page 51 and para.9.16 at page 68.

⁷⁰ The difference between the orientations of the ISC Code and the UK Stewardship Code has been overlooked even by British commentators. See for example Chiu & Katelouzou, *supra* note 7 at 134-135 ("The Code evolved out of the Institutional Shareholders' Committee's similarly-named Code of 2010, and therefore accords with market perceptions of the appropriate role for institutional investors.").

⁷¹ See however Arad Reisberg, *The Role of Institutional Shareholders: Stewardship and the Long-/Short-Termism Debate*, in Iris H-Y Chiu (ed.), *THE LAW ON CORPORATE GOVERNANCE IN BANKS* (Edward Elgar, 2015), 99, 124-126 (introducing views of mainly US and European scholars critical of the Kay Review).

⁷² Cheffins, *supra* note 40 at 1011.

⁷³ Cheffins, *supra* note 40 at 1018, 1023-1024. See also Lee Roach, *The UK Stewardship Code*,

envisaged by the Kay Review “will achieve anything of substance in the absence of some amendment of the liberal UK regime for takeovers, which induces corporate management to focus on the current share price and provides episodic but substantial pay-offs to shareholders”.⁷⁴ In this sense, Professor Davies states that the Kay Review “sits in the mainstream of the UK corporate governance tradition”.⁷⁵

Professors Chiu and Katelouzou attempt to depart from this mainstream by pointing out that “even where institutions support shareholder engagement, such engagement is on the basis of a shareholder value ideology that exerts short-termist pressures upon their investee companies and has deleterious effects upon corporate culture, bringing in short-termism and less regard for stakeholders and wider social responsibility”.⁷⁶ They criticize the UK Stewardship Code as “ideologically perplexed” for conceptualizing “investor-led governance within a public-interest framing” while continuing “to make overly optimistic assumptions about the motivations of different types of institutions and their alignment with socially beneficial effects in the long-term”.⁷⁷ At the same time, “the Code, being soft law, does not provide adequately for the accountability and governance mechanisms that would check and balance shareholders’ enhanced engagement roles and powers”.⁷⁸ From such a viewpoint, Professors Chiu and Katelouzou propose imposing mandatory disclosure requirements on institutional investors regarding their engagement intentions, plans and outcomes to the public, and regulatory standards of conduct focusing on “the long-term well-being of the company taking into account of other shareholders’ and stakeholders’ interest” via securities and investment regulation.⁷⁹ In contrast, Professor

11 JOURNAL OF CORPORATE LAW STUDIES 463, 469-471 (2011), Konstantinos Sergakis, *The UK Stewardship Code: Bridging the Gap between Companies and Institutional Investors*, 47 REVUE JURIDIQUE THÉMIS DE L’UNIVERSITÉ DE MONTREAL 109, at 133-134 (2013) and Reisberg, *supra* note 23 at 236-247.

⁷⁴ Paul Davies, *Shareholders in the United Kingdom*, in Jennifer G. Hill & Randall S. Thomas (eds.), RESEARCH HANDBOOK ON SHAREHOLDER POWER (Edward Elgar, 2015) 355, at 375.

⁷⁵ *Ibid.*

⁷⁶ Chiu & Katelouzou, *supra* note 12 at 73-74.

⁷⁷ Chiu & Katelouzou, *supra* note 12 at 87

⁷⁸ Chiu & Katelouzou, *supra* note 12 at 88.

⁷⁹ Chiu & Katelouzou, *supra* note 12 at 90-92, 94-96. See also Chiu & Katelouzou, *supra* note 7 at 151-152 (discussing the then-proposed Shareholder Rights Directive of the European Union and calling for complete “hardening” of the soft law of shareholder stewardship” while pointing out that “policy-makers need to be more honest and open about the regulatory

Reisberg suggests providing financial incentives through weighted dividends or tax benefits to reward worthy stewardship by long-term investors.⁸⁰

Professors Chiu and Katelouzou go on to assert that other countries including Japan have adopted stewardship codes from “the common concern” about “minority shareholder activism, especially of the offensive variant” “especially due to its perceived short-term nature and its likely negative impact on corporate wealth in general”.⁸¹ To ascertain whether this statement is correct, this Article next analyzes the text and the backgrounds of the Japanese Stewardship Code.

III. THE TRANSPLANT OF STEWARDSHIP CODES: THE CASE OF JAPAN

A. How is the Japanese Stewardship Code Different from the UK Code?

Japan adopted its stewardship code in February 2014, and later revised it in May 2017. The framework of the Japanese Stewardship Code is heavily influenced by the UK Stewardship Code. It takes the form of soft law; it is not mandatory for institutional investors to sign up to the code. If an institutional investor chooses to sign up, it is only required to comply with the principles and guidance of the Code, or to explain why it does not do so.⁸² The seven principles of the Japanese Code were also drafted by first translating those of the UK Code into Japanese and then considering one by one whether any modifications or additions were necessary to meet the circumstances in Japan.⁸³

objectives and premises underlying such legalisation of institutional shareholder duties.”). For similar arguments in the United States, see Usha Rodrigues, *Corporate Governance in an Age of Separation of Ownership from Ownership*, 95 MINNESOTA LAW REVIEW 1822 (2011) (asserting that shareholder empowerment and disclosure requirements introduced by the Dodd-Frank Act cannot solve the issue of short-termism and that substantive governmental regulation such as limitation on executive compensation is a better choice).

⁸⁰ Reisberg, *supra* note 23 at 249-250. See also, Sergakis, *supra* note 73 at 146-147.

⁸¹ Chiu & Katelouzou, *supra* note 7 at 135, 138. See also *ibid.* at 139 (stating that stewardship codes have been “further internationalised to address the need for constructive engagement by institutional investors for the purposes of supporting a long-term wealth-creating corporate sector and mitigating short-termism and trading-focused investment management, and the need to define the terms of engagement in order to rein in opportunistic activist behavior.”).

⁸² The 2017 Revised Japanese Code, *supra* note 2 at para.11-12 at page 6.

⁸³ See Document No.3 of the Third Meeting of the Council of Experts Concerning the Japanese

1. The Principles

The content of the Japanese Stewardship Code, however, is not identical to that of the UK Code. The principles of the Japanese Code are as follows:⁸⁴

So as to promote sustainable growth of the investee company and enhance the medium- and long-term investment return of clients and beneficiaries,

- 1. Institutional investors should have a clear policy on how they fulfill their stewardship responsibilities, and publicly disclose it.*
- 2. Institutional investors should have a clear policy on how they manage conflicts of interest in fulfilling their stewardship responsibilities and publicly disclose it.*
- 3. Institutional investors should monitor investee companies so that they can appropriately fulfill their stewardship responsibilities with an orientation towards the sustainable growth of the companies.*
- 4. Institutional investors should seek to arrive at an understanding in common with investee companies and work to solve problems through constructive engagement with investee companies.*
- 5. Institutional investors should have a clear policy on voting and disclosure of voting activity. The policy on voting should not be comprised only of a mechanical checklist; it should be designed to contribute to the sustainable growth of investee companies.*
- 6. Institutional investors in principle should report periodically on how they fulfill their stewardship responsibilities, including their voting responsibilities, to their clients and beneficiaries.*
- 7. To contribute positively to the sustainable growth of investee companies, institutional investors should have in-depth knowledge of the investee companies and their business environment and skills and resources*

Version of the Stewardship Code, submitted by the Secretariat (available at https://www.fsa.go.jp/en/refer/councils/stewardship/material/20131018_1.pdf).

⁸⁴ The 2017 Revised Japanese Code, *supra* note 2, the Principles of the Code at page 8. The principles remain unchanged from the original 2014 version. See the 2014 Japanese Code, *supra* note 2 at page 6.

needed to appropriately engage with the companies and make proper judgments in fulfilling their stewardship activities.

Principles 1, 2 and 6 of the Japanese Stewardship Code are substantially the same as Principles 1, 2 and 7 of the UK Code. However, the other parts of the Japanese Stewardship Code differ from the UK Code in that they appear to apply less investors' pressure on investee companies.⁸⁵

To begin with, the chapeau of the Japanese principles puts sustainable growth of the investee company ahead of the enhancement of the medium- and long-term investment return of clients and beneficiaries; whereas the UK Code only refers to the interest of the ultimate beneficiaries.

Secondly, while Principles 4 and 5 of the UK Code refer to the possibility of escalating stewardship activities when necessary, and recommend that institutional investors act collectively with other investors, no such reference can be found in the Japanese principles.⁸⁶ Instead,

⁸⁵ The following paragraphs are based on the analysis of Wataru Tanaka, *Nihon-ban suchuwadoshippu codo no kento: Kikan-toshika no yakuwari nitsuite no anbivarento na mikata* [An Analysis of the Japanese Stewardship Code: An Ambivalent View on the Role of Institutional Investors], 629 KANSAYAKU 66 at 68-69 (2014).

⁸⁶ At the second meeting of the Council of Experts Concerning the Japanese Version of the Stewardship Code, Mr. Muneaki Tokunari of Mitsubishi UFJ Trust and Banking Corporation, as the representative of trust banks that are often in charge of management of private pension funds, stated that in the then-current practice his bank asks investee companies for more explanation in certain occasions but does not have a concrete guideline on escalating the level of stewardship activities and that the banks does not participate in collective engagement. Mr. Toshinao Matsushima of Daiwa Asset Management, as the representative of the mutual funds industry, also made a similar statement. See the Minutes of the 2nd Council of Experts Concerning the Japanese Version of the Stewardship Code, at pages 12-13 and 15-16 (available at http://www.fsa.go.jp/en/refer/councils/stewardship/material/20130918_3.pdf). Based on these presentations, FSA proposed to deviate from the UK Code in this regard. See the Minutes of the 3rd Council of Experts Concerning the Japanese Version of the Stewardship Code, at page 13 (available at http://www.fsa.go.jp/en/refer/councils/stewardship/material/20131018_2.pdf).

While there was some support for making no reference to the possibility of escalating the level of stewardship activities as it would not fit the Japanese practice (ibid. at page 18), a few members of the Council expressed positive views on collective engagement and criticized the FSA's proposal (ibid. at page 19-20). It must be noted that, as a partial response, FSA issued a document on its interpretation of Japanese law on "acting in concert" under the large shareholding report requirement and the tender offer rules to remove legal ambiguities that may hinder collective engagement. FINANCIAL SERVICES AGENCY, CLARIFICATION OF LEGAL ISSUES RELATED TO THE DEVELOPMENT OF THE JAPAN'S STEWARDSHIP CODE (February 26, 2014, available at

Principle 4 of the Japanese Code requests institutional investors to arrive at a common understanding with investee companies, and to work with them in solving problems. It must be noted that the FSA admitted that sometimes it would be necessary to take more aggressive measures than merely asking for explanation and such measures are not excluded as a way of solving problems.⁸⁷ Still, the wording of Principle 4 may have the effect of giving Japanese companies room to argue that institutional investors requesting certain actions, such as an increase in payouts, are not making sufficient efforts to reach such a common understanding. In a similar vein, Principle 7 calls on institutional investors to have in-depth knowledge of investee companies and their business environment, as well as skills and resources necessary for appropriate engagement – again in order to contribute to the sustainable growth of investee companies.

Further, while Principle 3 of the English version of the Japanese Code requests institutional investors to “monitor” investee companies, as does that of the UK Code, the original Japanese document does not use the literal Japanese translation of the term “monitor”; instead it requests investors to “properly grasp the circumstances of investee companies”.⁸⁸ Together with the reference to “the sustainable growth of investee companies” in the same principle, the Japanese wording is milder and more nuanced – not encouraging institutional investors to take a tough stance against investee companies.

Overall, the Japanese principles can be described as being much friendlier to investee companies as compared to the UK principles.⁸⁹ This divergence from the UK Code has been

<http://www.fsa.go.jp/en/refer/councils/stewardship/20140226.pdf>). For the 2017 revision of the Japanese Stewardship Code that added some reference to collective engagement in the guidance section, see *infra* note 130 and accompanying text.

⁸⁷ THE COUNCIL OF EXPERTS CONCERNING THE JAPANESE VERSION OF THE STEWARDSHIP CODE, *supra* note 18 at Comment no.15 at page 4.

⁸⁸ This change in phrasing has been influenced by a remark at the 3rd meeting of the Council by Mr. Takaaki Eguchi, who had been involved in engagement and voting at large foreign institutional investors, stating that the term “monitoring” is not appropriate here as it suggest a “one-way surveillance” while the focus of the Council is promotion of “the long-term growth of investee companies, thereby building a win-win relationship between institutional investors and their investee companies”. See the Minutes of the 3rd Council of Experts Concerning the Japanese Version of the Stewardship Code, *supra* note 86 at page 17.

⁸⁹ Principle 5 of the Japanese Code also differs from Principle 6 of the UK Code as the second sentence of the former explicitly discourages the use of a mechanical checklist as a voting policy, which is accompanied by a paragraph in the guidance section stating that when “institutional investors use the service of proxy advisors, they should not mechanically depend on the advisors’ recommendations”. The 2014 Japanese Code, *supra* note 2, Paragraph 5-4 at page 11. However, this may not be so large a difference from the UK Code

criticized by some academics,⁹⁰ but welcomed by industries as reflecting the reality of Japanese corporate governance system,⁹¹ which traditionally focused on the interest of stakeholders, especially employees.⁹²

2. The Preface

Unlike the UK Code, the preface to the Japanese Stewardship Code prioritizes the enhancement of “the medium- to long-term investment return for their clients and beneficiaries” as the goal of stewardship responsibility and regards sustainable growth of investee companies as its metric, as mentioned earlier in Part I, Section C. Thus, the Japanese Stewardship Code also harbors some inconsistency between its preface and principles, albeit in a different manner from the UK Code, the preface of which emphasizes the long-term success of investee companies to the contrary.

as the fourth paragraph of the Guidance to Principle 6, which was added by the 2012 revision, also requires that institutional investors to “disclose the use made, if any, of proxy voting or other voting advisory services” and “describe the scope of such services, identify the providers and disclose the extent to which they follow, rely upon or use recommendations made by such services”.

⁹⁰ See for example, Wataru Tanaka, *Koporeto gabanansu no kanten kara mita nihonban suchuwadoshippu kodo – Eikoku kodo tonon sai ni chakumoku shite* [The Japanese Stewardship Code from the Perspective of Corporate Governance: With Focus on the Differences between the UK Code], 1 SHINTAKU FORAMU 35, at 38 (2014) (criticizing the emphasis of the sustainable growth of investee companies in the principles of the Japanese Stewardship Code as such idea would sometimes contradict with the interest of clients and ultimate beneficiaries).

⁹¹ See for example, Jun’ichi Kawada, *Kigyo saido no taio – JX Horudhingusu no baai* [Reactions of Companies to the Japanese Stewardship Code: The Case of JX Holdings], KIGYO KAIKEI Vol.66, No.8 (2014), 33 at 34-35. Mr. Kawada was a member of the Council of Experts Concerning the Japanese Version of the Stewardship Code and a director and senior vice president of JX Holdings, Inc. On the other hand, some academics have criticized the Japanese Code on this point. See for example, Tanaka, *supra* note 85 at 69 (asserting that the Japanese Code obscures, possibly intentionally, the fact that the interest of ultimate beneficiaries could conflict with that of investee companies, which could occur in a scenario such as when the company does not have an investment opportunity with returns exceeding investors’ cost of capital).

⁹² For detailed description of the traditional Japanese corporate governance system, see Zenichi Shishido, *Japanese Corporate Governance: The Hidden Problems of Corporate Law and Their Solutions*, 25 DELAWARE JOURNAL OF CORPORATE LAW 189 (2000) and Gregory Jackson & Hideaki Miyajima, *Introduction: The Diversity and Change of Corporate Governance in Japan*, in Masahiko Aoki, Gregory Jackson & Hideaki Miyajima (eds.), CORPORATE GOVERNANCE IN JAPAN: INSTITUTIONAL CHANGE AND ORGANIZATIONAL DIVERSITY (Oxford University Press, 2007), at 1, 3-6.

The question arising from this difference is, why the Japanese Stewardship Code is structured differently from the UK Code despite their apparent similarity. Let us now turn to the background of the Japanese Stewardship Code to examine its intended goal.

B. Background

1. Japan Revitalization Strategy: June 2013

As the background of establishing the Council of Experts Concerning the Japanese Version of the Stewardship Code, the preface of the Japanese Stewardship Code cites a document titled “the Japan Revitalization Strategy”.⁹³

This document was prepared by the Headquarters for Japan’s Economic Revitalization⁹⁴ as part of the Abe administration’s policies aimed at economic growth in the 2013 fiscal year. It claims that bold investment by private sector is necessary to promote innovation and that better corporate governance is required to support such “aggressive” management.⁹⁵ The adoption of a Japanese version of a stewardship code is listed as one of the representative measures that needs to be implemented swiftly.⁹⁶ In particular, the Japan Revitalization Strategy states as follows:

With the aim of promoting sustainable growth of companies, discuss and establish the principles for a wide range of institutional investors to appropriately discharge their stewardship responsibilities through constructive dialogues with invested companies by the end of this year while considering discussion of the Council on Economic and

⁹³ The 2014 Japanese Code, *supra* note 2, paragraphs 2-3 at page 1-2. No change is made to these paragraphs in the 2017 version.

⁹⁴ The Headquarters for Japan’s Economic Revitalization (*Nihon Keizai Saisei Honbu*) is a body established by the Abe administration by a cabinet decision on December 26, 2012, and consists of all ministers with the Prime Minister as its chief. Its mandate is to plan and to coordinate economic policies of the government as a whole. See, http://japan.kantei.go.jp/96_abe/decisions/2012/1226saiseihonbu_e.html.

⁹⁵ JAPAN REVITALIZATION STRATEGY – JAPAN IS BACK (June 14, 2013) (available at https://www.kantei.go.jp/jp/singi/keizaisaisei/pdf/en_saikou_jpn_hon.pdf) at page 36-37.

⁹⁶ JAPAN REVITALIZATION STRATEGY, *supra* note 95 at 14, 16.

*Fiscal Policy concerning the market economy system in Japan.*⁹⁷

It should be noted that the phrase “sustainable growth of companies” had already appeared at this stage as “the aim” for adopting a stewardship code. The document itself, however, does not provide any explanation on the reason for such a mandate.⁹⁸ On the other hand, the adoption of a stewardship code is listed together with other measures such as the promotion of appointment of independent directors and the creation of a new stock index consisting of high-profile companies in terms of profitability and management,⁹⁹ making it difficult to ascertain the orientation of the document. The same problem applies to the order made by Prime Minister Abe on April 2, 2013 at the sixth meeting of the Headquarters for Japan’s Economic Revitalization. It calls on the Minister for Financial Services to “coordinate with other relevant ministers and consider, with the aim of promoting the sustainable growth of companies, principles for a wide range of institutional investors to appropriately discharge their stewardship responsibilities”.¹⁰⁰

2. Industrial Competitiveness Council: March 2013

Interestingly, discussions held a few months earlier at the Industrial Competitiveness Council,¹⁰¹ which is mentioned in the preface of the Japanese Stewardship Code as the basis of the order by Prime Minister Abe cited above,¹⁰² were a little different.

On March 15, 2013, at the fourth meeting of the Industrial Competitiveness Council, the introduction of a Japanese version of the UK Stewardship Code was proposed by members of the Council from the private sector as one of the measures to promote the replacement of obsolete

⁹⁷ JAPAN REVITALIZATION STRATEGY, *supra* note 95 at 37.

⁹⁸ The same problem applies to the order made by Prime Minister Abe at the 6th meeting of the Headquarters for Japan’s Economic Revitalization, which is also cited in the preface of the Japanese Stewardship Code. See the 2014 Japanese Code, paragraph 1 at page 1.

⁹⁹ JAPAN REVITALIZATION STRATEGY, *supra* note 95 at 37-38.

¹⁰⁰ As cited by the 2014 Japanese Code, *supra* note 2 at paragraph 1 at page 1.

¹⁰¹ The Industrial Competitiveness Council (*Sangyo Kyosoryoku Kaigi*) was established by the Headquarters for Japan’s Economic Revitalization on January 8, 2013 to consider specific measures for economic growth and consisted of the Prime Minister, the Vice Prime Minister, the Minister for Economic and Fiscal Policy, the Cabinet Secretary, the Minister of Economy, Trade and Industry, and members appointed from the industry and academics. See <https://www.kantei.go.jp/jp/singi/keizaisaisei/skkkaigi/konkyo.html>.

¹⁰² The 2014 Japanese Code, *supra* note 2 at paragraph 1 at page 1.

industries and businesses by new ones.¹⁰³ Here, the stewardship code was described as a mechanism to compel institutional investors to play an active role – but no additional details about its goals were provided (e.g., such as promoting sustainable growth of investee companies).¹⁰⁴

On the contrary, Mr. Takeshi Niinami, the then-CEO of a major convenience store chain Lawson, emphasized the necessity of interventions by institutional investors. In particular, he stated as follows:

Mr. Niinami: It is important to have external discipline of the management by the stock market, namely by outspoken shareholders.¹⁰⁵ Non-activist institutional investors as shareholders with a mid- to long-term perspective should properly intervene in management of companies to promote replacement of outdated industries and businesses by new ones. In this regard, the government should consider introducing a Japanese version of the UK's Stewardship Code so that the private sector cannot make excuses for failing to act.¹⁰⁶

The ministers at the meeting did not object to Mr. Niinami's statement on the role of institutional investors.¹⁰⁷ However, at a subgroup meeting of the Industrial Competitiveness

¹⁰³ See Document No.1 of the Fourth Meeting of the Industrial Competitiveness Council, submitted by Mr. Masahiro Sakane as the chair of the subgroup on the promotion of replacement of outdated industries and businesses, at page 2 (available in Japanese at <https://www.kantei.go.jp/jp/singi/keizaisaisei/skkkaigi/dai4/siryou1.pdf>).

¹⁰⁴ Document No. 3 of the Sixth Meeting of the Headquarters for Japan's Economic Revitalization, The Issues Raised by at the Fourth and the Fifth Meetings of the Industrial Competitiveness Council by Members from the Private Sector (available in Japanese at <https://www.kantei.go.jp/jp/singi/keizaisaisei/dai6/siryou03.pdf>), at page 1.

¹⁰⁵ The term “outspoken shareholders” is the literal English translation of the Japanese term used in Mr. Niinami's remark, “*mono iu kabunushi*”. This term, which is often used in Japanese media, is usually translated as “shareholder activists”, but the author chose the term “outspoken shareholders” as the second sentence of Mr. Niinami's remark seems to differentiate institutional investors from activists.

¹⁰⁶ The Minutes of the Fourth Meeting of the Industrial Competitiveness Council (March 15, 2013), at page 5 (available in Japanese at <https://www.kantei.go.jp/jp/singi/keizaisaisei/skkkaigi/dai4/gijiroku.pdf>).

¹⁰⁷ See, the Minutes of the Fourth Meeting of the Industrial Competitiveness Council, *supra* note 106 at page 5-10. In contrast, Professor Heizo Takenaka expressed his support for Mr. Niinami (*ibid.* at page 11).

Council held earlier on March 6, 2013, where Mr. Niinami proposed the introduction of a stewardship code for the first time, Mr. Akira Amari, then the Minister for Economic and Fiscal Policy and the Minister for Economic Revitalization disagreed with Mr. Niinami.¹⁰⁸

Minister Amari: Investors have gradually become less patient and the period from their investment to exit is getting shorter and shorter. To respond to requests from activist shareholders to payout retained earnings, companies should, for example, be permitted to pay more dividends to shareholders that have held shares for a longer period of time. It would be impossible to attract long-term investment when investors that had only recently bought shares can easily pressure companies and make off with retained earnings that have been accrued over time. Although investors are becoming more and more short-termed oriented across the world, Japan should establish a system that attracts long-term investment. Otherwise, R&D-intensive firms cannot prosper.¹⁰⁹

Mr. Niinami responded with the assertion that return on equity of Japanese companies had not increased in the long term despite their allegedly long-term management approach, and that activist shareholders are necessary to some extent to improve corporate value by exerting pressure on companies to give reasonable explanations for the usage of cash they are hoarding.¹¹⁰ This view of Mr. Niinami, however, substantially differs from the basic orientation of the UK Stewardship Code, which focuses on public interest by restraining excessive risk-taking and

¹⁰⁸ The Summary of the Discussions at the Meeting on March 6, 2013 of the Subgroup of the Industrial Competitiveness Council on Specific Topics, at page 3 (available in Japanese at https://www.kantei.go.jp/jp/singi/keizaisaisei/kaigou/pdf/h250306_gijiyousi.pdf) (Mr. Niinami arguing that “it is necessary to make rigorous systems, such as the UK Stewardship Code, in order to achieve higher productivity of firms” and to have “institutional investors such as Government Pension Investment Fund monitor corporate governance of companies more rigorously” and referring to a practice of General Electric that it “only pursues segments in which they can become the leader or the second in that market within a few years”).

¹⁰⁹ The Summary of the Discussions at the Meeting on March 6, 2013 of the Subgroup of the Industrial Competitiveness Council on Specific Topics, *supra* note 108 at page 5-6.

¹¹⁰ The Summary of the Discussions at the Meeting on March 6, 2013 of the Subgroup of the Industrial Competitiveness Council on Specific Topics, *supra* note 108 at page 6. Mr. Yasuchika Hasegawa, then the president of Takeda Pharmaceutical Co., Ltd., also expressed a similar view that the management of a company is responsible to explain to its shareholders why the company is holding retained earnings. *Ibid.*

short-termism.¹¹¹ In contrast, Mr. Amari's view appears to be largely congruent with the UK Code.

This interesting exchange suggests the following two points. First, Mr. Niinami's true intention seems not to be in favor of adopting the UK Stewardship Code as such, but rather in importing the UK practice of engagement by institutional shareholders for effective discipline of management. Second, Minister Amari's anti-activist view seems to be the background of the insertion of the phrase "with the aim of promoting sustainable growth of companies" into the Japan Revitalization Strategy.

3. Council on Economic and Fiscal Policy: April 2013

Minister Amari's anti-activist orientation is also reflected in the role he played in the Council on Economic Fiscal Policy.¹¹² On April 18, 2013, about one month after the fourth meeting of the Industrial Competitiveness Council, Mr. Jyoji (George) Hara was invited to the eighth meeting of the Council on Economic Fiscal Policy to make a presentation on establishing "a market economy system that enables sustainable growth".¹¹³ He criticized US-style corporate governance as focusing only on the interests of shareholders and management, and advocated that companies should be evaluated not by return on equity, but by its sustainability, distributive fairness and improvements in its business.¹¹⁴ He also made various proposals, such as the restriction of stock-

¹¹¹ See Part II, Section B.

¹¹² The Council on Economic and Fiscal Policy (*Keizai Zaisei Shimon Kaigi*) was originally established in 2001 pursuant to Article 18, paragraph 1 of the Act for Establishment of Cabinet Office (Act. No.89 of 1999). The core mission of this council is to discuss important issues regarding economic and fiscal policy as consulted by the Prime Minister or the Minister on Economic and Fiscal Policy. Article 19, paragraph 1, no.1 and paragraph 2, Act for Establishment of Cabinet Office. The Minister on Economic and Fiscal Policy is an *ex officio* member of the Council and is to chair the meeting of the Council when the Prime Minister is absent. Article 21, paragraph 4 and Article 22, paragraph 1, no.2, Act for Establishment of Cabinet Office.

¹¹³ Mr. Jyoji (George) Hara is a venture capitalist based in the United States and the chairman of the board of directors of a non-governmental organization Alliance Forum Foundation, which criticizes shareholder-primacy and advocates an idea named "public interest capitalism". See http://www.allianceforum.org/en/profile/?cnt=cnt_01 and http://www.allianceforum.org/en/capitalism/?cnt=cnt_01.

¹¹⁴ The Minutes of the 8th Meeting of 2013 of the Council on Economic and Fiscal Policy, at page 5-6 (available in Japanese at <http://www5.cao.go.jp/keizai-shimon/kaigi/minutes/2013/0418/gijiroku.pdf>).

based compensation and share repurchases, together with the introduction of preferential treatment of mid- to long-term shareholders.¹¹⁵

Following the lines of Mr. Hara's presentation, Minister Amari then proposed establishing an expert group under the Council to conduct research on a "desirable market economy system" that "enables sustainable growth through appropriate allocation of capital and distribution of profits".¹¹⁶ Accordingly, the Expert Committee on Desirable Market Economy System (*Mezasubeki shijyo keizai shisutemu ni kansuru senmon chosakai*) was established,¹¹⁷ and the Japan Revitalization Strategy explicitly directed that the discussions of this committee must be taken into consideration when drafting the Japanese Stewardship Code.¹¹⁸

The final report of the Expert Committee, which was published on November 1, 2013, emphasizes that "corporate governance prioritizing adjustments of the interests of various stakeholders" is necessary in order to "improve the overall corporate value from a medium- and long-term perspective".¹¹⁹ It also asserts that institutional investors should "fulfill fiduciary responsibility by taking into account improvement of the overall corporate value in the medium and long terms, instead of leaning excessively toward maximization of short-term shareholder returns".¹²⁰ From such a perspective, this report calls for the adoption of the Japanese Stewardship Code based on "the circumstances in Japan, with a focus placed on the achievement

¹¹⁵ The Minutes of the 8th Meeting of 2013 of the Council on Economic and Fiscal Policy, *supra* note 114 at page 8.

¹¹⁶ Document No.2 of the 8th Meeting of 2013 of the Council on Economic and Fiscal Policy, submitted by the Minister on Economic and Fiscal Policy (available in Japanese at http://www5.cao.go.jp/keizai-shimon/kaigi/minutes/2013/0418/shiryo_02.pdf).

¹¹⁷ Summary of discussions and documents of the Experts Committee on Desirable Market Economy System are available in Japanese at <http://www5.cao.go.jp/keizai-shimon/kaigi/special/market/index.html>.

¹¹⁸ See *supra* note 97 and accompanying text.

¹¹⁹ REPORT BY THE EXPERT COMMITTEE ON DESIRABLE MARKET ECONOMY SYSTEM (November 1, 2013), at page 12 (available at <http://www5.cao.go.jp/keizai-shimon/kaigi/special/market/report.pdf>).

¹²⁰ *Ibid.* The overall corporate value is defined as "a broad concept that does not merely refer to ordinary monetary value (so-called shareholder value) but also includes elements difficult to measure in numerical terms, such as value arising from external economies and diseconomies whose monetary value cannot be evaluated immediately (reduction of environmental burden, etc.) and value relating to uncertain future sustainability (measures concerning exhaustible resources, etc.)". *Ibid.* at page 9-10.

of sustainable growth of companies through constructive communications between institutional investors and companies”.¹²¹

When the Council of Experts Concerning the Japanese Version of the Stewardship Code heard this final report at its fourth meeting held on November 27, 2013, Professor Wataru Tanaka criticized the Final Report for not supporting its arguments with factual evidence necessary to convince “readers who may view such arguments as a means to give an excuse for the currently stagnant profitability”.¹²² Mr. Masaya Sakuma, the Director of Economic, Fiscal and Social Structure of the Cabinet Office in charge of the secretariat of the Expert Committee on Desirable Market Economy System, responded that the report “does not intend to criticize short-term investment at all” as it also “refers to the need to maintain ‘liquidity’ in transactions” in the market, and that it is not the intention of the report “to use our argument about short-termism and the lack of medium to long-term funding as an excuse for the stagnant state of profitability”.¹²³

At the end of his remarks, however, Mr. Sakuma also stated that the “Committee was in a sense initiated by a concept similar to Public Interest Capitalism as noted by Mr. Hara, Deputy Chairman of the committee. In view of such background, I would appreciate your understanding as to the difficulty we faced in putting ideas together as the secretariat to the CEFPP Committee.”¹²⁴ This statement of Mr. Sakuma arguably suggests that the orientation of the Final Report was already determined by a political initiative of Minister Amari to promote Mr. Hara’s view from the Expert Committee’s inception, and thus that it was impossible to alter the final outcome of the discussions, even though the government officials in charge might not have been completely convinced.

4. Other Corporate Governance Reforms Around the Same Period

The above analysis depicts the existence of two camps with different views on the role of pressure from shareholders (i.e., one represented by Mr. Niinami and the other by Minister Amari) that led

¹²¹ *Ibid.* at page 14.

¹²² See the Minutes of the Fourth Meeting of the Council of Experts on the Stewardship Code, at page 5 (available at <http://www.fsa.go.jp/en/refer/councils/stewardship/minutes/20131127.pdf>).

¹²³ The Minutes of the Fourth Meeting of the Council of Experts on the Stewardship Code, *supra* note 122 at page 5.

¹²⁴ *Ibid.*

to the adoption of the Japanese Stewardship Code. This sub-section analyzes other corporate governance reforms around the same period as a way to illuminate which camp was ultimately more influential.¹²⁵ To state the conclusion upfront, it appears from the recent corporate governance reforms that the camp promoting more shareholder pressure to discipline management has prevailed¹²⁶ – supporting Mr. Niinami’s, not Minister Amari’s, point of view.

First, it has been clarified through the public comment process that the Japanese Stewardship Code does not prohibit institutional investors from requesting investee companies to increase dividends.¹²⁷ Institutional investors are expected to consider whether such a request fits within their overall stewardship responsibilities in the particular context. Further, the Japanese Stewardship Code was revised in 2017,¹²⁸ placing more emphasis on the pressure of institutional investors on investee companies.¹²⁹ For example, a paragraph on collective engagement, to which no reference was made in the original 2014 text, is added in the guidance section to Principle 4, stating that “it would be beneficial for” institutional investors “to engage with investee companies in collaboration with other institutional investors (collective engagement) as necessary”.¹³⁰ Under the 2017 Revised Code, institutional investors are also required to disclose how they have

¹²⁵ See Kansaku, *supra* note 14 at 1012-1013 (stating that the Japanese Stewardship Code was adopted as part of the so-called “growth strategy” of the Abe administration which aims to improve corporate governance and to promote corporate value).

¹²⁶ An earlier report published in 2009 by a study group established by the Financial Services Agency also emphasized the importance of exercise of voting rights based on fiduciary duty of institutional investors and disclosure of their voting results. At this time, there was no mention to the sustainable growth of investee companies. See, REPORT BY THE FINANCIAL SYSTEMS COUNCIL’S STUDY GROUP ON THE INTERNATIONALIZATION OF JAPANESE FINANCIAL AND CAPITAL MARKETS ~ TOWARD STRONGER CORPORATE GOVERNANCE OF PUBLICLY LISTED COMPANIES (June 17, 2009) at 15-16, available at <https://www.fsa.go.jp/en/news/2009/20090618-1/01.pdf>.

¹²⁷ The Council of Experts Concerning the Japanese Version of the Stewardship Code, *supra* note 18, Comment No.3 at page 1.

¹²⁸ For the 2017 revision of the Japanese Stewardship Code, see generally, Yasumasa Tahara, Hiroshi Someya & Keita Yasui, *Suchuwadoshippu codo kaitei no kaisetsu* [Commentaries on the Revision of the Stewardship Code], 2138 SHOJIHOMU 15 (2017) (in Japanese).

¹²⁹ The 2017 revision has added “opportunities arising from social and environmental matters” as one of the factors that institutional investors should “monitor” or “grasp” at Guidance 3-3. In the author’s view, however, this amendment is not so meaningful as the original 2014 text already listed “risks arising from social and environmental matters” in the same paragraph.

¹³⁰ The 2017 Revised Japanese Code, *supra* note 2, Guidance 4-4, at page 13.

voted on each agenda item at shareholders' meetings of individual investee companies.¹³¹ In addition, the revision emphasizes the role of asset owners such as pension funds in stewardship activities,¹³² calls for effective control of conflicts of interest of asset managers, especially those belonging to financial conglomerates,¹³³ and requires institutional investors which have a passive governance strategy to participate in engagement and voting more actively.¹³⁴

Second, the Japanese government has succeeded in nudging Japanese listed companies to appoint at least one or two outside/independent directors through measures such as the 2014 Reform of the Companies Act and the 2015 Japanese Corporate Governance Code, which introduced "comply or explain" rules regarding appointment of one outside director or two independent directors, respectively.¹³⁵ One of the roles expected to be performed by these outside and/or independent directors is to represent the interests of shareholders in the boardroom and to function as a barrier insulating the management from the interests of core employees.¹³⁶

Third, the Japanese government has also been trying to tackle the issue of "cross-shareholdings".¹³⁷ One characteristic of traditional Japanese listed companies is that a large

¹³¹ The 2017 Revised Japanese Code, *supra* note 2, Guidance 5-3, at page 15. This individual disclosure requirement was not included in the original 2014 version due to the objections from the industry and some investors. Kansaku, *supra* note 11 at 19. The revised code, however, decided to override such objections and to introduce this requirement in order to enhance the transparency of the stewardship activities of asset managers and to eliminate concerns on conflicts of interest of asset managers who belong to financial conglomerates. See, the 2017 Revised Japanese Stewardship Code, at page 15, note 15.

¹³² The 2017 Revised Japanese Code, *supra* note 2, Guidance 1-3, 1-4 & 1-5 at page 9-10.

¹³³ The 2017 Revised Japanese Code, *supra* note 2, Guidance 2-2, 2-3, & 2-4 at page 11.

¹³⁴ The 2017 Revised Japanese Code, *supra* note 2, Guidance 4-2 at page 13.

¹³⁵ For details of the recent Japanese reforms on board independence, see Gen Goto, Manabu Matsunaka & Souichirou Kozuka, *Japan's Gradual Reception of Independent Directors: An Empirical and Political-Economic Analysis*, in: Dan W. Puchniak, Harald Baum & Luke Nottage (eds.), *INDEPENDENT DIRECTORS IN ASIA* (Cambridge University Press, 2017) at 135 and Gen Goto, *Recent Boardroom Reforms in Japan and the Roles of Outside/Independent Directors*, in Hiroshi Oda (ed.), *COMPARATIVE CORPORATE GOVERNANCE: THE CASE OF JAPAN*, Journal of Japanese Law, Special Issue No.12 (Carl Heymanns/Wolters Kluwer, 2018) at 33.

¹³⁶ Goto, *supra* note 135 at 50-51. See also, Franz Waldenberger, 'Growth Oriented' Corporate Governance Reform – Can It Solve Japan's Performance Puzzle?, 29 JAPAN FORUM 354, 366-369 (2017) (describing the disadvantages of the predominance of in-house careers in Japanese companies).

¹³⁷ For the effect and the current state of cross-shareholdings in Japan, see Gen Goto, *Legally "Strong" Shareholders of Japan*, 3 MICHIGAN JOURNAL OF PRIVATE EQUITY AND VENTURE

proportion of their shares, often the majority, was held by “stable shareholders”, which consisted of the company’s banks and friendly business partners.¹³⁸ Since such shareholders have an incentive to support the management of the company in order to maintain good business relationships, this ownership structure effectively insulated managers from the pressure of capital markets. Seeing such phenomenon as problematic as it arguably leads to inefficiency and managerial slack, the 2015 Japanese Corporate Governance Code provides that Japanese listed companies shall disclose their policy on cross-shareholding, and provide an annual detailed explanation on the objective and rationale behind major cross-shareholdings after examining their mid- to long-term economic rationale.¹³⁹ The 2018 revision of the Japanese Corporate Governance Code further seeks to accelerate the reduction of cross-shareholdings by adding a supplementary principle calling on companies not to discourage their shareholders from divesting their shareholding by, for example, suggesting that such divestments would result in reduction of business transactions with them.¹⁴⁰

It is also worth noting that the so-called “Ito Review”, a report commissioned by the Ministry of Economy, Trade and Industry to Professor Kunio Ito under inspiration from the Kay Review,¹⁴¹ rather emphasizes the importance of Japanese companies achieving a level of return on equity that exceeds the cost of capital required by global investors, so that the Japanese market can attract capital to support investment for long-term innovation.¹⁴² Such an emphasis on return on equity clearly differs from Mr. Hara’s stakeholder-oriented view.¹⁴³

CAPITAL LAW 125 142-146, 149-152 (2014).

¹³⁸ This situation is also called “cross-shareholding”, as such a relationship is often mutual.

¹³⁹ Principle 1-4, Japanese Corporate Governance Code.

¹⁴⁰ Supplementary Principle 1.4.1, the Revised Japanese Corporate Governance Code, at page 7, available at https://www.jpx.co.jp/english/news/1020/b5b4pj000000jvxxr-att/20180602_en.pdf.

¹⁴¹ See an interview with Prof. Kunio Ito by MARR Online, available at https://www.marr.jp/etc/hen_interview/entry/4793 (stating that the launch of the “Ito Review” project on July 2013 was greatly inspired by the Kay Review published one year before).

¹⁴² THE ITO REVIEW OF COMPETITIVENESS AND INCENTIVES FOR SUSTAINABLE GROWTH – BUILDING FAVORABLE RELATIONSHIPS BETWEEN COMPANIES AND INVESTORS– FINAL REPORT (August 2014), at page 7-9 (available at http://www.meti.go.jp/english/press/2014/pdf/0806_04b.pdf).

¹⁴³ See *supra* note 113-114 and accompanying texts.

5. Summary: The Goal of the Japanese Stewardship Code

The above analysis shows that the adoption of the Japanese Stewardship Code was part of a recent trend of corporate governance reforms in Japan aimed at more effective discipline of management for the purpose of meeting shareholders' interests – in line with Mr. Niinami's initial rationale for proposing the code. In this context, it appears clear that the insertion of the phrase “with the aim of promoting sustainable growth of companies” was not the driving force behind the Code. Rather it was a compromise to appease those who resisted the trend towards a more shareholder-oriented system of corporate governance.

From this perspective, the goal of the Japanese Stewardship Code is to change the behavior of domestic institutional investors, in particular life insurance companies and some investment trust management companies which have been criticized for their reluctance to take a tough stance against management due to their business relationships with investee companies.¹⁴⁴ In contrast, foreign institutional investors, who are often viewed in Japan as being free from conflict of interests and being unreluctant to exert pressure on the management of investee companies when necessary,¹⁴⁵ are not the main target of the Japanese Stewardship Code. Stated

¹⁴⁴ For example, Professor Kenjiro Egashira lists the inactivity of domestic institutional investors as one of the basic foundations of traditional Japanese corporate governance system and claims that the 2014 Reform of the Companies Act introducing the “comply or explain” rule on appointment of at least one outside director would fail to change the behavior of Japanese listed companies as long as domestic institutional investors stay the same. See Kenjiro Egashira, *Kaishaho no kaisei ni yotte nihon no kaisha ha kawaranai* [Japanese Companies Would Not Change Regardless of the Companies Act Reform], *HORITSU JIHO*, Vol.86, No.11, at 59, 60 (2014). One recent empirical study reports that the ratio of shareholding by domestic institutional investors has a positive effect on the probability of hedge fund activism internationally, but a negative effect in Japan (both effects were statistically significant). Marco Becht, Julian Franks, Jeremy Grant & Hannes F. Wagner, *Returns to Hedge Fund Activism: An International Study*, 30 *REVIEW OF FINANCIAL STUDIES* 2933, at 2946-2948 (2017). It must be noted, however, that the unwillingness of investment managers to take actions that are disfavored by corporate managers is not unique to Japan. See Bebchuk, Cohen & Hirst, *supra* note 5 at 21-23 (describing the similar attitude of investment managers in the United States).

¹⁴⁵ Professor Hideaki Miyajima and his colleagues report that, after controlling for reverse causality, higher shareholding by foreign investors in Japanese companies facilitates appointment of independent directors, affects corporate policy on investment, capital structure and payout, and has positive impact on ROA and Tobin's Q of investee companies. See Hideaki Miyajima, Takaaki Hoda & Ryo Ogawa, *Does Ownership Really Matter? The Role of Foreign Investors in Corporate Governance in Japan* (2015, available at <https://www.rieti.go.jp/jp/publications/dp/15e078.pdf>) and Hideaki Miyajima & Ryo Ogawa, *Convergence or Emerging Diversity? Understanding the Impact of Foreign Investors on*

differently, the Japanese Stewardship Code aims to make domestic institutional investors act like foreign institutional investors. Reflecting such an orientation, the Japanese Stewardship Code has been criticized for not covering cross-shareholdings by banks and non-financial companies,¹⁴⁶ whereas the UK Stewardship Code was criticized by Professor Cheffins for not including foreign investors in its scope.¹⁴⁷

C. The True Difference between the Japanese and the UK Codes

In summary, although the Japanese Stewardship Code and the UK Stewardship Code may bear superficial resemblance due to their broad focus on the same two core concepts, their fundamental policy rationales are almost diametrically opposed. The UK Stewardship Code aims to restrain excessive risk-taking and short-termism by making institutional investors more responsible to the public. Conversely, the Japanese Stewardship Code intends to champion shareholders' interests by making domestic institutional investors more active shareholders who would exert pressure on entrenched management.¹⁴⁸

Corporate Governance in Japan (2016, available at <https://www.rieti.go.jp/jp/publications/dp/16e053.pdf>). For international research with similar findings, see also, Stuart Gillan & Laura T. Starks, *Corporate Governance, Corporate Ownership, and the Role of Institutional Investors: A Global Perspective*, 13 JOURNAL OF APPLIED FINANCE 4 (2003) and Jan Bena, Miguel A. Ferreira, Pedro P. Matos & Pedro Pires, *Are Foreign Investors Locusts? The Long-Term Effects of Foreign Institutional Ownership*, 126 JOURNAL OF FINANCIAL ECONOMICS 122 (2017).

¹⁴⁶ Sadakazu Osaki, *Nihon-ban kodo seiko no jyoken* [The Japanese Code's Conditions for Success], KIGYO KAIKEI, Vol.66, No.8, at 48, 51-52 (2014), Ryohei Nakagawa, *Shareholding Characteristics and Imperfect Coverage of the Stewardship Code in Japan*, 29 JAPAN FORUM 338, at 346 (2017). See also *supra* note 137-140 and accompanying text (discussing the principles of the Japanese Corporate Governance Code on cross-shareholdings).

¹⁴⁷ See *supra* note 73 and accompanying text.

¹⁴⁸ It must be noted that at the third meeting of the Council of Experts Concerning the Japanese Version of the Stewardship Code, the Financial Services Agency as the secretariat of the Council described that the statement of the Japan Revitalization Strategy referring to "the aim of promoting the sustainable growth of companies" and the language in the preface to the 2012 Revised UK Stewardship Code aiming to "promote the long-term success of companies in such a way that the ultimate providers of capital (managed by institutional investors) also prosper" "do not contradict each other". See, Document No.3 of the Third Meeting of the Council of Experts Concerning the Japanese Version of the Stewardship Code, submitted by the Secretariat (available at https://www.fsa.go.jp/en/refer/councils/stewardship/material/20131018_1.pdf) at page 1. While this description does not conform perfectly with the view explained in the text, it does

It is worth emphasizing, however, that the Japanese Stewardship Code “primarily targets institutional investors investing in Japanese listed shares”.¹⁴⁹ This focus, which is similar to the UK Code’s, suggests that the Japanese Government’s objective in adopting the Stewardship Code was to improve the corporate governance of Japanese listed companies, rather than to promote the interests of Japan’s ultimate beneficiaries.¹⁵⁰ This may sound superficially similar to the goal of the UK Code. Nevertheless, this goal of the Japanese Stewardship Code is still different than that of the UK Code, as the former aims to prioritize the interests of shareholders over other stakeholders, especially employees.¹⁵¹

This difference in the basic orientations of the Japanese and the UK Stewardship Codes has been largely overlooked,¹⁵² even by Professor Hiroyuki Kansaku, who chaired the Council of

not preclude the possibility that the secretariat deliberately avoided pointing out the divergence between the UK Code and the Japan Revitalization Strategy, which might have provoked controversies over the goal to be aimed at.

¹⁴⁹ The 2017 Revised Japanese Code, *supra* note 2, para.8 at page 5 (unchanged from the 2014 original Code).

¹⁵⁰ If the goal of the Japanese Stewardship Code were to promote the interests of Japanese ultimate beneficiaries, then it should target institutional investors funded by Japanese interest investing in non-Japanese listed shares as well.

¹⁵¹ In a separate piece on recent Japanese reforms on board independence, the author discusses that one of the various roles expected to be performed by outside/independent directors is to represent the interests of shareholders in the boardroom and to function as a barrier insulating the management from the interests of core employees who may oppose decisions such as divestment of non-core businesses. See Goto, *supra* note 135 at 50-51.

¹⁵² See for example, Yoko Manzawa, *Suchuwadoshippu sekinin to jyutakusha sekinin – Eibei ni okeru kangaekata no hikaku no kokoromi* [Stewardship Responsibility and Fiduciary Duty: A Comparison with the Anglo-American Way of Thinking], 2070 SHOJIHOMU 23, at 24, 32 note 6 (2015) (stating that the Japanese Code and the UK Code are the same as both codes require institutional investors to promote the growth of investee companies and the interest of their beneficiaries, although there is a slight difference in the wording) and Nakagawa, *supra* note at 349 (stating that making institutional investors less speculative is “the whole intention of deploying the stewardship rules”).

A notable exception is the view of Mr. Sadakazu Osaki of Nomura Research Institute, who briefly but correctly observes the difference of the goals of the two stewardship codes. See Sadakazu Osaki, *The New Stewardship Code in Japan: Comparison with the UK Code and its Implementation*, in Hiroshi Oda (ed.), *COMPARATIVE CORPORATE GOVERNANCE: THE CASE OF JAPAN*, Journal of Japanese Law, Special Issue No.12 (Carl Heymanns/Wolters Kluwer, 2018) at 101, 102-103. Professor Mika Takahashi also states that “the Japanese Stewardship Code is not based on a radical criticism against the short-termism as in the United Kingdom” and “puts itself in line with fiduciary duty” as it aims to “enlarge the mid- to long-term investment return to the clients and beneficiaries of institutional investors”. Professor Takahashi, however, does not provide the background for such a difference between Japan

Experts Concerning the Japanese Version of the Stewardship Code.¹⁵³ Also, Professor Wataru Tanaka, who was a member of the Council, focused only on the principles of the Japanese and the UK Codes, and erroneously states that the concept of the sustainable growth of investee companies does not exist in the UK Code.¹⁵⁴ In a similar vein, in the international discourse, Professors Bebchuk, Cohen and Hirst portrayed the stewardship codes of the United Kingdom, Japan, and Canada as attempts to solve the agency problem of institutional investors,¹⁵⁵ a conclusion that is correct in Japan's case but not for the UK.

In contrast, Professor Chiu provides a UK-biased view¹⁵⁶ by stating that the Japanese Stewardship Code “could be seen as providing an ex ante form of defence against more unpredictable forms of shareholder activism”, despite her recognition that the Japanese Code “is purportedly introduced as part of a package of measures to revitalize the Japanese economy and to improve the investment appeal of its listed sector”.¹⁵⁷ Also, Professors Fenwick and Vermeulen, who have recently conducted a survey on the regulatory environment of engagement by

and the UK. See Mika Takahashi, ‘*Jyutakusha no chui gimu*’ to *suchuwadoshippu sekinin* [‘Fiduciary’s Duty of Care’ and Stewardship Responsibility], 2 SHINTAKU FORAMU 45, at 49 (2014).

In the international discourse, Professor Jennifer Hill correctly notes that while the UK Stewardship Code seeks to meet “the need for effective risk control in the post-crisis era”, the Japanese Stewardship Code focuses “on arresting declining profitability, unlocking value and increasing investor returns” and deliberately creates “a ‘warmer climate’ for foreign investors and shareholder activists”. HILL, *supra* note 3 at 20, 22. She, however, fails to explain the whole picture underlying the Japanese Code as she views the reference to the concepts of “sustainable growth” and “medium to long-term corporate value” is a reflection of the above goal of the Japanese Code, and does not explain why the Japanese Code envisages relatively gentle kind of shareholder engagement. *Ibid.* at 22, 23. As noted earlier, these concepts and the relatively gentle stance were included in the Japanese Code rather as a compromise to appease those who resisted shareholder-oriented system. See *supra* Part III, Section B, 5.

¹⁵³ See Kansaku, *supra* note 11 at 18-20 (listing characteristics of the Japanese Code in comparison with the UK Code).

¹⁵⁴ Tanaka, *supra* note 85 at 69.

¹⁵⁵ Bebchuk, Cohen & Hirst, *supra* note 5 at 108.

¹⁵⁶ In the same vein, the view of this article could be criticized as Japan-biased. The author's point is not to discuss which one of the two is more appropriate or authentic but to emphasize the importance of recognizing a possible home-country bias of an observer.

¹⁵⁷ Iris H-Y Chiu, *Learning from the UK in the Proposed Shareholder Rights Directive 2014? European Corporate Governance Regulation from a UK Perspective*, 114 ZEITSCHRIFT FÜR VERGLEICHENDE RECHTSWISSENSCHAFT 121, at 150-151 (2015).

institutional investors in various countries, state that “shareholders, particularly institutional investors, must be viewed as ‘stewards’ of the *company*” and observe that stewardship codes in general “attempt to create more responsible and purposeful investor engagement” and that the “Japanese Stewardship Code is modeled after the UK code”.¹⁵⁸ The finding of this Article shows that the value of studies such as Fenwick and Vermeulen’s would be diminished unless enough attention is paid to the context behind the adoption of stewardship codes in each country.

IV. THE EFFECTS AND THE LIMITS OF STEWARDSHIP CODES

A. The Effects and the Limits of Stewardship Codes

1. Different Goals, Different Effects and Limits

When the goals of stewardship codes differ, as seen in the case of the UK Code and the Japanese Code, their effectiveness and limits could also differ. Thus, the effectiveness of each stewardship code must be evaluated individually, taking into consideration possible differences in the goals of each.

In the United Kingdom, the goal of a stewardship code is to advance the public interest by restraining excessive risk-taking and investor short-termism. There, the problem is that institutional investors acting as loyal “stewards” of their clients and ultimate beneficiaries would not act in furtherance of such public interest when doing so does not coincide with the interest of their clients and ultimate beneficiaries. In other words, this goal is incompatible with the logic of stewardship that requires institutional investors to be loyal to the interests of their ultimate beneficiaries.

It is from such a viewpoint that Professors Chiu and Katelouzou propose imposing disclosure requirements and regulatory standards of conduct on institutional investors instead of introducing a stewardship code; in similar vein, Professor Reisberg proposes to provide weighted

¹⁵⁸ Fenwick & Vermeulen, *supra* note 3 at 10, 36 (emphasis added by the author). It is also worth noting that Professors Fenwick and Vermeulen summarize the goal of the Japanese Stewardship Code somewhat roughly as “(1) to discharge its responsibility to facilitate the continuous growth of the invested company and (2) to try to increase the medium-term or long-term return of the beneficial owners and clients of the institutional investor”, thereby ignoring the priority provided in the preface of the Japanese Code. See *ibid.* at 36 and *supra* note 18 and accompanying text.

dividends or tax benefits to long-term shareholders.¹⁵⁹ While the desirability of some of these proposals remain debatable, they seem to be at least more consistent with their goal of restraining excessive risk-taking and investor short-termism when compared with the UK Stewardship Code.

In contrast, the goal of the Japanese Stewardship Code is more effective discipline of management from the viewpoint of shareholders' interests by urging domestic institutional investors to act for the benefit of the ultimate beneficiaries. This goal is compatible with the logic of stewardship where institutional investors are the fiduciaries of ultimate beneficiaries. In this context, the key issue becomes the effective enforcement of fiduciary duties, in particular, the duties of loyalty and care.¹⁶⁰ After taking a brief look at the current status of the adoption of the Japanese Stewardship Code by institutional investors, the remainder of this part will analyze the effect and limits of the Code from this perspective.

2. Signatories to the Japanese Stewardship Code

The Japanese Stewardship Code requests institutional investors who have adopted the Code to notify the Financial Services Agency (FSA) accordingly, and the FSA to publicize the list of such institutional investors ("signatories" to the Code).¹⁶¹ Table 1 below shows the composition of these signatories as of April 5, 2018.¹⁶²

Table 1: Signatories to the Japanese Stewardship Code as of April 5, 2018

Types of signatories	Number of signatories
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¹⁵⁹ See *supra* note 76-80 and accompanying texts.

¹⁶⁰ The Kay Review states that the "core fiduciary duties are those of loyalty and prudence" and that "effective stewardship is possible only if ... the steward proceeds on the basis of obligations of loyalty and prudence". The Kay Review: Final Report, *supra* note 61, para.9.6-9.8 at 66. See also, the Myners Report, *supra* note 40 at 92-93 (asserting that all pension fund trustees and the UK law should incorporate the principle of the US Department of Labor's Interpretative Bulletin, which states that the "fiduciary obligations of prudence and loyalty to plan participants and beneficiaries require the responsible fiduciary to vote proxies on issues that may affect the value of the plan's investment".).

¹⁶¹ The 2014 Japanese Code, *supra* note 2, para.14 at page 4, and the 2017 Revised Japanese Code, *supra* note 2, para.13 at page 6-7.

¹⁶² FINANCIAL SERVICES AGENCY, LIST OF INSTITUTIONAL INVESTORS SIGNING UP TO "PRINCIPLES FOR RESPONSIBLE INSTITUTIONAL INVESTORS" «JAPAN'S STEWARDSHIP CODE» (April 5, 2018), available at https://www.fsa.go.jp/en/refer/councils/stewardship/20180405/en_list_01.pdf.

Trust banks	6
Investment managers (mutual funds and investment advisors)	162
Pension funds	30
Insurance companies	22
Other institutions (including proxy advisors)	7
Total	227

These signatories include most of Japan’s major domestic trust banks and insurance companies, whereas adoption by Japan’s private pension funds is limited.¹⁶³

Out of the 162 investment managers (mutual funds and investment advisors), 48 are foreign institutions.¹⁶⁴ Among them are several activist hedge funds including Brandes Investment Partners, Dalton Investments, Effissimo Capital Management, and Oasis Management Company. Some Japanese activists, such as SPARX Asset Management Co. and Strategic Capital, also have signed up. In addition, there are four foreign pension funds, namely, CalPERS, Fourth Swedish National Pension Fund, UK Railway Pension Trustee Company Limited, and the University of California.

While the number of signatories itself does not guarantee the effectiveness of the Stewardship Code in improving the quality of institutional investors’ engagement,¹⁶⁵ it is still noteworthy that foreign institutional investors, especially activist hedge funds, took the trouble of signing up to the Japanese Stewardship Code, which features rather investee company-friendly principles and guidance.¹⁶⁶ One possible reason for this move is that by signing up, these investors are trying to portray themselves as long-term investors supportive of the “sustainable

¹⁶³ Ryoko Ueda, *Nihonban suchuwadoshippu kodo no kaitei ~ Kikantoshika no yakuwari to jikkosei no kyoka* [The Revision of the Japanese Stewardship Code: The Role of Institutional Investors and Strengthening of Its Effectiveness], 382 SHIHONSHIJO 26 at 30 (2017). For private pension funds, see also *infra* note 196-205 and accompanying texts.

¹⁶⁴ This is judged by their lack of corporate numbers assigned to legal persons established under Japanese law. Corporate numbers of signatories are only shown in the Japanese version of the list of signatories. See https://www.fsa.go.jp/singi/stewardship/list/20180405/list_01.pdf.

¹⁶⁵ Reisberg, *supra* note 23 at 224-226. See also, Sergakis, *supra* note 73 at 136.

¹⁶⁶ See *supra* note 84-89 and accompanying texts.

growth of investee companies” and to dilute their image as hostile activists.¹⁶⁷ This tactics, however, may not be that effective as companies are unlikely to be so naïve as to believe in a declaration of this sort that is not supported by formal sanctions.

B. Duty of Loyalty and Conflicts of Interest

1. Institutional Investors and Conflicts of Interest

Turning back to the analysis of the effects and limits of the Japanese Stewardship Code, the essence of the duty of loyalty of fiduciaries is that fiduciaries must put the interests of their beneficiaries ahead of their own.¹⁶⁸ Thus, the core issue for a stewardship code from the duty-of-loyalty perspective is managing the effect of conflicts of interest between institutional investors and their ultimate beneficiaries. Accordingly, Principle 2 of the Japanese Stewardship Code, in conformity with Principle 2 of the UK Code, requests institutional investors to “have a clear policy on how they manage conflicts of interest in fulfilling their stewardship responsibilities and publicly disclose it”.

A conflict of interest is particularly likely to occur when an institutional investor offers financial services to its investee companies, or when it is affiliated with companies that offer financial services to investee companies.¹⁶⁹ For example, a life insurance company may undertake management of an investee company’s pension fund, or an investment advisor could be a subsidiary of a bank making a loan to its subsidiary’s investee company. In such cases, institutional investors might face pressure not to vote against the management of investee companies so as to avoid losing valuable contracts for themselves or their affiliated companies’ other businesses.

On the assumption that institutional investors have not done enough to manage conflicts of interest, the 2017 revision of the Japanese Stewardship Code has added a few

¹⁶⁷ See Tanaka, *supra* note 90 at 37-38 (suggesting that, if the Japanese Stewardship Code had taken more adversarial stance, Japanese domestic institutions would have been more reluctant to sign up to the Code).

¹⁶⁸ See Guidance 2-1, the 2017 Revised Japanese Code, *supra* note 2 (stating that “institutional investors should put the interest of their client and beneficiary first”)and Guidance to Principle 2, the 2012 Revised UK Code, *supra* note 1 (“An institutional investor’s duty is to act in the interest of its clients and/or beneficiaries.”).

¹⁶⁹ Black & Coffee, *supra* note 5 at 2059-2061.

sentences to the Guidance to Principle 2 requesting institutional investors to make their policies on conflict of interest more specific and to establish governance structures to prevent conflict of interest, such as independent committees on voting of shares.¹⁷⁰

2. Disclosure of Voting Records on Individual Agenda of Each Investee Company

As voting of shares is an important aspect of stewardship activities by institutional investors, the Japanese Stewardship Code has a separate principle on this issue, requesting institutional investors to “have a clear policy on voting and disclosure of voting activity”,¹⁷¹ again in line with the UK Code.¹⁷²

One of the most controversial issues that arose in the process of the 2017 revision was whether institutional investors should disclose how they have voted on the individual agenda of each investee company, or whether it is sufficient to disclose their voting records on an aggregate basis. In the end, disclosure of voting results on the level of individual agenda was adopted as Guidance 5-3 to address conflicts of interest in the Japanese market,¹⁷³ overriding oppositions from some institutional investors and listed companies arguing that such individual disclosure may encourage institutional investors to follow formalistic voting standards, which in turn may hinder meaningful dialogue between institutional investors and investee companies.¹⁷⁴

Major domestic trust banks and investment managers belonging to large financial conglomerates quickly accepted the request of Guidance 5-3 on individual disclosure, presumably in response to the criticism on the high-likelihood of conflict of interest in financial

¹⁷⁰ The 2017 Revised Japanese Code, *supra* note 2, Guidance 2-2 and 2-3. See also, Tahara et al., *supra* note 128 at 18-19.

¹⁷¹ The 2017 Revised Japanese Code, *supra* note 2, Principle 5.

¹⁷² The 2012 Revised UK Code, *supra* note 1, Principle 6, the 2012 UK Stewardship Code.

¹⁷³ The 2017 Revised Japanese Code, *supra* note 2, note 15 at page 15, Tahara et al., *supra* note 128 at 21. The UK Stewardship Code does not explicitly require disclosure of voting records on individual agenda, but it is reported that major institutional investors in the United Kingdom do so for the sake of better accountability and management of conflict of interest. *Ibid.*

¹⁷⁴ The 2017 Revised Japanese Code, *supra* note 2, note 15 at page 15, Hiroki Sanpei, *Giketsuken koshi kekka no kaiji* [Disclosure of Voting Results], 1515 JURISUTO 22, at 26 (2018).

conglomerates.¹⁷⁵ In contrast, two of the four largest life insurance companies have not decided to disclose individual voting results as of April 2018.¹⁷⁶ In lieu of individual disclosure, Nippon Life Insurance, the largest life insurer in Japan, has established an independent advisory council on stewardship activities, which is comprised of one independent director, two academics, and one lawyer, to oversee the voting process and how the company should vote on important cases.¹⁷⁷ Such an independent committee is one possible solution for issues of conflicts of interest;¹⁷⁸ whether it works effectively will in turn depend on whether the committee is adequately monitoring.

What then is the effect of the individual disclosure requirement by the 2017 revision? Although there is no systematic empirical study on this issue to the best of the author's knowledge as of April 2018,¹⁷⁹ there are some anecdotal evidences suggesting that such disclosure

¹⁷⁵ Osamu Hamada, *Giketsuken koshi kekka no kobetsu kaiji wo meguru giron to kikan toshika no taio jyokyo* [Discussions on the Disclosure of Individual Voting Results and the Responses of Institutional Investors], 2145 SHOJHOMU 37, at 40-41 (2017), Naoyoshi Ema, *Kikan toshika ni yoru giketsuken koshi no jyokyo – 2017-nen no kabunushi sokai wo furikaette* [The Current State of Voting of Shares by Institutional Investors: Looking Back at Shareholders' Meetings in 2017], 2150 SHOJHOMU 13, at 14 (2017), Sanpei, *supra* note 174 at 23.

¹⁷⁶ It might be worth noting that these two life insurance companies, namely Nippon Life Insurance and Meiji Yasuda Life Insurance, take the form of mutual insurance company instead of stock corporation. In this case, profits of insurance company through services offered to investee companies substantially belong to insurance policyholders as the equity holders of a mutual insurance company. Thus, conflicts of interest between beneficiaries and insurance company would not be as strong as in the case of insurance companies taking the form of a stock corporation.

¹⁷⁷ Nihon Seimei Sogo Gaisha, *Suchuwadoshippu katsudo no kyoka ni muketa "Suchuwadoshippu shimon iinnkai" no shinsetsu oyobi kongo no katsudo hoshin ni tsuite* [Establishment of "the Advisory Council on Stewardship" and Future Action Plans toward Improvement of Stewardship Activities], March 30, 2009, available at <https://www.nissay.co.jp/news/2016/pdf/20170330.pdf>.

¹⁷⁸ Simon CY Wong, *How Conflicts of Interest Thwart Institutional Investor Stewardship*, BUTTERWORTHS JOURNAL OF INTERNATIONAL BANKING AND FINANCIAL LAW, September 2011, 481, at 482.

¹⁷⁹ See Hamada, *supra* note 175 at 42, 43 note 22 (citing a descriptive statistic reporting that at shareholders' meetings held of companies comprising Nikkei 225 index in June 2017, the amount of decrease of the average ratio of votes supporting proposals made by the management, except for those on anti-takeover measures, was less than one percentage point). See also, Yasutomo Tsukioka, *The Impact of Japan's Stewardship Code on Shareholder Voting* (2017, available at <https://ssrn.com/abstract=3013999>) (studying the effects of the original Japanese Stewardship Code using data of investee companies from 2010 to 2016 on the ratio of votes for and against for agenda on appointment of directors).

matters.¹⁸⁰ For example, Mitsubishi UFJ Trust Bank disclosed that it had voted against the reelection of directors of Mitsubishi Motors in December 2016, which was surprising as both companies belong to Mitsubishi group, one of the six largest *keiretsu* known for its strong group unity.¹⁸¹ Also, in June 2017, Mizuho Trust Bank supported a shareholder's proposal that was opposed by the management of its parent company, Mizuho Financial Group.¹⁸²

C. Duty of Care and Business Models of Investors

The duty of care requires institutional investors as fiduciaries to exercise reasonable care when they perform their task. The core task is of course to invest the fund they manage, and the investment strategy of institutional investors differ depending on their "business model".

In the same vein, stewardship activities of these investors would also differ rationally depending of their business model and investment strategy.¹⁸³ For example, investors with a concentrated portfolio would actively engage with the management to raise the firm value of their investee companies.¹⁸⁴ However, active engagement is not a rational choice for a passive fund

¹⁸⁰ Hamada, *supra* note 175 at 41.

¹⁸¹ *Mitsubishi UFJ Shintaku, Mitsubishi Jidosha no jinjian ni "no" Toshi no ronri zenmenni* [Mitsubishi UFJ Trust votes against the nomination of directors in Mitsubishi Motors: The Logic of Investment Comes to Front], NIHON KEIZAI SHINBUN, 2017/5/31 22:30JST (https://www.nikkei.com/article/DGXLASDC31H1Z_R30C17A5EE9000/). While the shareholders' meeting in question was held before the revision of the Japanese Stewardship Code, disclosure of individual voting records had been already proposed by another council at the Financial Services Agency on November 30, 2016. See, the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code Opinion Statement No. 3, Effective Stewardship Activities of Institutional Investors – To Enhance Constructive Dialogue toward Sustainable Corporate Growth, page 3-4 (November 30, 2016, available at https://www.fsa.go.jp/en/refer/councils/follow-up/statements_3.pdf).

¹⁸² *Giketsuken koshi de oyagaisha ni "hanki" Asemame Wan nado* [Rising in "Revolt" against the Parent Company in Voting of Shares: Asset Management One and Others], NIHON KEIZAI SHINBUN, 2017/8/30 19:59 JST (https://www.nikkei.com/article/DGXLASGD30H5H_Q7A830C1EE9000/).

¹⁸³ Serdar Celik & Mats Isaakson, *Institutional Investors as Owners: Who Are They and What Do They Do?*, OECD Corporate Governance Working Papers, No.11 (2013, available at <http://dx.doi.org/10.1787/5k3v1dvmfk42-en>), at 5, 22-27, John C. Coates IV, *Thirty Years of Evolution in the Roles of Institutional Investors in Corporate Governance*, in Jennifer G. Hill & Randall S. Thomas (eds.), RESEARCH HANDBOOK ON SHAREHOLDER POWER (Edward Elgar, 2015), 79, at 85-86.

¹⁸⁴ Takaaki Eguchi, *Tayo na toshika, tayō na gabanansu koka – Passibu unyō no kakudai ga*

aiming to fully replicate a certain market index, the business model of which is to provide diversified investment at a low cost.¹⁸⁵

As long as there is no conflict of interest, and as long as clients of institutional investors have entrusted their funds knowing the latter's business model, such diversity of type and intensity is not problematic from the viewpoint of the interest of ultimate beneficiaries. In other words, the type and intensity of stewardship activities could and should be left to the discretion of each institutional investor as part of their business model and investment strategy, as long as conflict of interest is effectively managed.

However, from the perspective of the Japanese Government, whose aim is to make Japanese companies to prioritize the interest of shareholders over that of stakeholders by utilizing the pressure from institutional investors,¹⁸⁶ passivity on stewardship activity of some institutional investors would be problematic. Thus, the 2017 revision of the Japanese Stewardship Code has added a new paragraph requesting passive funds "to actively take charge of engagement and voting",¹⁸⁷ although such active engagement might not be in the best interest of clients of such funds. In other words, the goal of the Japanese Stewardship Code is not perfectly compatible with the logic of stewardship as fiduciaries of ultimate beneficiaries.¹⁸⁸

imisuru mono [Diverse Investors, Diverse Governance Effects: The Meaning of the Expansion of Passive Investment], in Hiroyuki Kansaku (ed.), KIGYO HOSEI NO SHORAI TENBO – SHIHON SHIJO SEIDO NO KAIKAKU HENO TEIGEN – 2018-NENDO BAN [Future Prospects of Enterprise Law: Proposals on Reforms of the Capital Market System, 2018 edition] (Shihonshijo Kenkyukai, 2018), 415, at 422-423.

¹⁸⁵ See Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Cost of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUMBIA LAW REVIEW 863, 866, 868-869, 889-895, Bebchuk, Cohen & Hirst, *supra* note 5 at 97-98, 100-101, 108 and Curtis J. Milhaupt, *Evaluating Abe's Third Arrow: How Significant Are Japan's Recent Corporate Governance Reforms?*, in Hiroshi Oda (ed.), COMPARATIVE CORPORATE GOVERNANCE: THE CASE OF JAPAN, Journal of Japanese Law, Special Issue No.12 (Carl Heymanns/Wolters Kluwer, 2018) at 65, 74. For a similar view in Japan, see Takahito Kato, *Suchuwadoshippu kodo no rironteki kousatsu – Kikan toshika no insenthibu kozo no kanten kara* [A Theoretical Analysis of the Stewardship Code: From the Perspective of the Incentive Structure of Institutional Investors], 1515 JURISUTO 16, 18-21 (2018).

¹⁸⁶ See *supra* Part III, Section C.

¹⁸⁷ The 2017 Revised Japanese Code, *supra* note 2, Guidance 4-2. See also Tahara et al., *supra* note 128 at 20.

¹⁸⁸ See also Celik & Isaakson, *supra* note 183 at 21 ("Before we discuss these different determinants of shareholder engagement it is important to remind ourselves why the degree of ownership engagement is a public policy concern. Why should policy makers care? From a public policy perspective, ownership engagement is not a moral issue. Nor can it be seen as a

Would then the Japanese Stewardship Code be effective? On one hand, there is a possibility that the Stewardship Code may be entirely ignored¹⁸⁹ or result only in formalistic engagement that does not produce value.¹⁹⁰ On the other hand, the Stewardship Code could “serve as a focal point for changing the norms about asset management and capital productivity in Japan”.¹⁹¹ While it is still too early to have definitive empirical evidence, anecdotal evidences described in the previous section on voting behavior by large trust banks show that the latter effect may be more than a pipe dream.

D. Monitoring and Enforcement

The Japanese Stewardship Code takes the form of “comply or explain”. As signing up to the code does not guarantee either compliance or meaningful explanation, monitoring and enforcement from the viewpoint of ultimate beneficiaries is essential for the Stewardship Code to be effective.¹⁹² In particular, whether an institutional investor who declares compliance does comply, and whether an institutional investor who chooses to explain provides a persuasive explanation must be monitored.¹⁹³

general obligation or fiduciary duty that would override other objectives, such as maximizing the return to the institution’s ultimate beneficiary. What is primarily matters for public policy is the role that ownership engagement plays for effective capital allocation and the informed monitoring of corporate performance.”)

¹⁸⁹ Milhaupt, *supra* note 185 at 9 (noting that the Stewardship Code would be “practically useless” as many institutional investors “rationally do not engage”).

¹⁹⁰ Takaaki Eguchi, *Engejimento no jidai ni okeru kikan toshika no yakuwari – Nihon ni okeru atarasii toshikazo kochiku wo mezashite* [The Role of Institutional Investors in an Era of Engagement: Toward Building of a New Image of Investors in Japan], 2109 SHOJIHOMU 24, at 27 (2016).

¹⁹¹ Milhaupt, *supra* note 185 at 9. See also Wataru Tanaka, *Nihonban suchuwadoshippu kodo no kaitei* [The Revision of the Japanese Stewardship Code], 398 SIRYOBAN SHOJIHOMU 6, at 12 (2017) (asserting that by officially acknowledging the value of stewardship activities, the Stewardship Code might make coordination among institutional investors easier and thus solve the collective action problem).

¹⁹² One of the major concerns in Japan has been the weakness of the enforcement due to the Stewardship Code’s “comply or explain” approach and the lack of a specific enforcement mechanism. See Kansaku, *supra* note 14 at 1018-1019, Mayumi Takahashi, *Sofuto ro to shiten no koporeto gabanansu kodo to suchuwadoshippu kodo* [The Corporate Governance Code and the Stewardship Code as Soft Law], JIYU TO SEIGI, Vol.67, No.7, 41, at 45 (2016).

¹⁹³ While the data of the Financial Services Agency as of December 2016 shows that the ratio

The question is who would provide such monitoring. In this regard, the Japanese Stewardship Code follows the UK Code that divides institutional investors into two categories: asset managers, who are entrusted with the day-to-day management of funds provided by the other group; and asset owners such as pension funds and life insurance companies.¹⁹⁴ Both codes expect asset owners to monitor stewardship activities of asset managers as their direct clients.¹⁹⁵

It has been observed, however, that private pension funds have tended not to sign up to the Japanese Stewardship Code.¹⁹⁶ As of April 5, 2018, there are 30 pension-fund signatories, which comprise of 12 public pensions, 14 private pensions, and 4 foreign pension funds.¹⁹⁷ Out of the 14 private pension funds, 8 are of companies that are under the supervision of the FSA, such as banks and insurance companies, and 3 are associations of private pension funds.¹⁹⁸ This leaves only 3 signatories that are pension funds of individual companies, out of a total of 774 private pension funds as of April 1, 2018.¹⁹⁹

of “compliance” by signatories exceeds 90% for all seven principles, more specific requests in the guidance section may have a lower compliance rate. See Document No.3 of the First Meeting of the Council of Experts on the Stewardship Code submitted by the Financial Services Agency, Status of the Stewardship Code and Opinion Statement of the Follow-up Council (January 31, 2017), at page 6 and 19, available at https://www.fsa.go.jp/en/refer/councils/stewardship/material/20170131_3.pdf.

¹⁹⁴ The 2012 Revised UK Code, *supra* note 1, para.6 at page 1, the 2017 Revised Japanese Code, *supra* note 2, para.7 at page 5.

¹⁹⁵ The 2012 Revised UK Code, *supra* note 1, para.7 at page 2 (“Since asset owners are the primary audience of asset managers’ public statements as well as client reports on stewardship, asset owners should seek to hold their managers to account for their stewardship activities. In so doing, they better fulfil their duty to their beneficiaries to exercise stewardship over their assets.”), the 2017 Revised Japanese Code, *supra* note 2, Guidance 1-3, 1-4 and 1-5. See also Reisberg, *supra* note 23 at 241.

¹⁹⁶ Tahara et al., *supra* note 128 at 18. In contrast, public pension funds, in particular the Government Pension Investment Fund (GPIF), are very active on stewardship. See for example, GPIF, STEWARDSHIP PRINCIPLES & PROXY VOTING PRINCIPLES (June 1, 2017), available at http://www.gpif.go.jp/en/stewardship_and_esg/pdf/stewardship_principles_and_proxy_voting_principles.pdf.

¹⁹⁷ For the list of signatories, see Financial Services Agency, *supra* note 162.

¹⁹⁸ One of such association is the Pension Fund Association, which has been active in stewardship activities since early 2000s. See Bruce E. Aronson, *A Japanese CalPERS or a New Model for Institutional Investor Activism? Japan’s Pension Fund Association and the Emergence of Shareholder Activism in Japan*, 7 NYU JOURNAL OF LAW & BUSINESS 571 (2011).

¹⁹⁹ The three signatories are the pension funds of Eisai, Panasonic and Secom. The total number

The reason for the low adoption rate by pension funds seems to be threefold. First, most of the private pension funds are small in size, holding less than 10 billion Yen, and cannot afford to hire sufficient staffs for stewardship activities.²⁰⁰ Second, as the beneficiaries of private pension funds are employees, they cannot monitor such funds effectively due to collective action problems. And third, unlike trust banks or investment managers, private pension funds are not supervised by the Financial Services Agency and thus do not face regulatory pressure to sign up, except for those of financial companies which are regulated by the Agency.²⁰¹

Actually, the 2017 revision did take this issue into consideration, and added a few paragraphs in the guidance section to promote stewardship activities by asset owners.²⁰² The number of pension fund signatories after the revision, however, did not increase by much,²⁰³ suggesting that the Revised Code is unlikely to address such collective action problems. To urge private pension funds to be more active, encouragement from their regulator, the Ministry of Health, Labor and Welfare,²⁰⁴ is crucial.²⁰⁵ This may call for additional regulations, but for a

of private pension funds (774) is derived from adding the 32 employees' pension funds (*kosei nenkin kikin*) to the 742 fund-type defined-benefit corporate pensions (*kikin-gata kakutei kyufu kigyō nenkin*). See Kigyō Nenkin Rengokai (Pension Fund Association), *Kigyō nenkin no genkyō (Heisei 30-nen 4 gatsu 1 nichi genzai)* [The Current State of Corporate Pensions (as of April 1, 2018)] (April 9, 2018), available at <https://www.pfa.or.jp/activity/tokei/nenkin/files/genkyo.pdf>.

²⁰⁰ Ryoko Ueda, *Nihonban suchuwadoshippu kodo no kaitei ~ Kikantoshika no yakuwari to jikkosei no kyōka* [The Revision of the Japanese Stewardship Code: The Role of Institutional Investors and Strengthening of Its Effectiveness], 382 SHIHONSHIJO 26 at 30 (2017).

²⁰¹ Naoya Ariyoshi, *Suchuwadoshippu kodo kaitei heno jitsumu taio* [Practical Issues in Response to the Revision of the Stewardship Code], 2141 SHOJIHOMU 84, at 91 (2017).

²⁰² Tahara et al., *supra* note 128 at 17-18.

²⁰³ The number of pension-fund signatories as of December 27, 2016, the year before the 2017 revision, was 26.

²⁰⁴ The Ministry of Health, Labor and Welfare, in collaboration with the Pension Fund Association, has issued a report to foster adoption of the Stewardship Code by private pension funds. Suchuwadoshippu Kentokai (The Study Group on Stewardship), *Kigyō nenkin to nihonban suchuwadoshippu kodo* [Corporate Pensions and the Japanese Stewardship Code] (March 17, 2017), available at <https://www.pfa.or.jp/kanyo/shiryo/stewardship/houkoku/files/all.pdf>.

²⁰⁵ See also Ariyoshi, *supra* note 201 at 91 (asserting that it is not enough to rely on spontaneous adoption by private pension funds and suggesting that fiduciary duties of directors of such funds would call for adequate stewardship activities).

reason that is completely different from that in the UK.²⁰⁶

V. CONCLUSION

This article has demonstrated that there is a divergence between the basic goals and orientation of the Japanese and the UK Stewardship Codes, which has been largely overlooked in the literature. Although the term “stewardship” suggests that stewardship codes are based on the logic of a fiduciary duty compelling a fiduciary to act in the interest of its beneficiary, the goal of the UK Stewardship Code is instead to restrain excessive risk-taking and short-termism by making institutional investors more responsible to the public.

In contrast, the Japanese Stewardship Code aims to change the attitude of domestic institutional investors in order to make Japanese corporate governance more oriented towards the interests of shareholders rather than those of stakeholders. This goal of the Japanese Code is more compatible with the logic of stewardship than that of the UK Code. At the same time, the Japanese Government considers this goal to be in the public interest of Japan.

Another finding of this article is that different stewardship codes have different goals and that this must be taken into consideration when assessing their effectiveness. The success of the Japanese Stewardship Code will primarily depend on how well domestic institutional investors are incentivized to act in the interest of their ultimate beneficiaries and to monitor entrenched management. Conversely, the success of the UK Stewardship Code will likely depend on how well it can make institutional investors consider the interests of the public and of stakeholders other than shareholders. Regulatory interventions might be necessary in both cases, but for different reasons.

The diversity in the goals and measures of effectiveness of stewardship codes is the consequence of the variety in the systems and primary issues of corporate governance in each jurisdiction. This suggests that, although stewardship codes are proliferating around the world, what seems like a move towards convergence may actually be an evidence of continued divergence – with “stewardship” having different meanings in different jurisdictions. Thus, inter-jurisdictional comparisons of stewardship codes must be undertaken with caution, with a comparison of the text of the principles and guidance being only the starting point – and not the end - of any analysis. Ultimately, the policies driving the adoption of such codes and the specific

²⁰⁶ See *supra* note 159 and accompanying texts.

corporate governance context into which a stewardship code is implemented appear to be critical. As such, multiple jurisdiction-specific lenses are necessary when examining stewardship codes in a comparative context.