2019 17th
JCGR Corporate Governance Survey
<< JCGIndex Survey >>
Report

December 1, 2019

Japan Corporate Governance Research Institute

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JCGR Corporate Governance Survey Report 2019

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Introduction

The corporate governance reforms pursued under Abenomics have now raised expectations for corporate governance through the capital market. Recognizing that Japanese companies are no longer at the stage of introducing corporate governance, the Japan Corporate Governance Research Institute (JCGR) has started to conduct a new Corporate Governance Survey in 2019. This report outlines the results of the new annual Corporate Governance Survey 2019 (JCGIndex Survey 2019) that well reflects the new situation in Japan. We are grateful to all companies that responded to this survey.

The JCGR defines the period from 2002 to 2017 as Phase I, and the 16 surveys conducted in Phase I as Phase I Surveys. Surveys conducted in or after 2019 are defined as Phase II Surveys.

1. Background and results of this survey

Within a short period, corporate governance reforms have been implemented in an unprecedent scale under the second Abe administration's new Growth Strategy. The Financial Services Agency formulated Japan's Stewardship Code in 2014 (revised in 2017); the amendment of the Companies Act in 2015 introduced company with audit and supervisory committee; and the Tokyo Stock Exchange made the Corporate Governance Code part of its Securities Listing Regulations in 2015. The reforms expect institutional investors to enhance the investee companies' corporate value and sustainable growth through "purposeful dialog" of shareholders. For companies, five principles are proposed based on OECD's Principles of Corporate Governance, in expectation of rational and fair corporate governance under independent directors and internationally competitive management: a) Securing the Rights and Equal Treatment of Shareholders, b) Appropriate Cooperation with Stakeholders other than Shareholders, c) Ensuring Appropriate Information Disclosure and Transparency, d) Responsibilities of the Board, and e) Dialogue with Shareholders.

These reforms apply in fact a soft-law approach of "Comply or Explain", assuming an Anglo-Saxon rational stock market. It is questionable that the Japanese stock market is rational enough, but at any rate, corporate governance reforms are indispensable to regain Japan's international competitiveness, and worth public interests.

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Looking into the JCGIndex Survey for 2019 from this perspective, the results presented in this paper give us an impression that the corporate governance reforms are still yet to bear fruit. We hope that governance reforms will bring about management reforms, but it is hard to achieve the change in a short period since both governance and management are deeply tied to the society and history. Yet we have no other choice but to speedily address the drastic change the world is experiencing. The fact that hasty actions are undesirable cannot justify slowing down the reform. Investors, executives and all members of the public need to make a commitment to corporate governance.

2. Scope/period of this survey, and number of companies that responded

From September 2019 to October 2019, we surveyed all companies listed on the First Section of the Tokyo Stock Exchange (2,148, as of September 2, 2019), of which 165 responded to the survey. This time, 55 companies responded to the survey for the first time.

In Phase I, we received responses from 986 distinct companies (and a cumulative total of 3,260) throughout the surveys. The numbers of companies that responded to our survey for each year are as follows: 159 (2002), 201 (2003), 341 (2004), 405 (2005), 312 (2006), 311 (2007), 252 (2008), 215 (2009), 127 (2010), 120 (2011), 131 (2012), 120 (2013), 118 (2014), 147 (2015), 150 (2016) and 151 (2017).

3. Overview of questions

3.1 Governance model for current companies

Companies have social responsibility of serving for the benefits of all stakeholders—employees, managers, customers, suppliers, creditors, shareholders, governments, and local communities to name some— because the support from these stakeholders are necessary for the companies' existence. In the framework of joint-stock company, however, companies are in reality (not by law) treated as private property of shareholders, who contribute money to the company and in turn exercise the control over the company as owners. Moreover, they take responsibility for the consequences of the business by sharing retained earnings. Retained earnings is equal to the sales minus various expenses, and therefore risky (i.e. not predetermined at all). It is shareholders who bear this risk of business.

Joint-stock companies that operate large-scale business with money contribution from a large number of shareholders assume separation of ownership and management. Although shareholders do not directly participate in management, they instead elect directors at the shareholders' meeting and entrust the management to the board of directors. In the form of electing directors who realize business execution (in another word, management) in line with shareholders' interests, shareholders control companies. That is what governance by shareholders means. In most countries under such a system, board of directors makes important decisions on business, and selects CEO and other executive officers (as for Japan, representative directors are selected in companies with board of corporate auditors and companies with audit and supervisory committee, and executive officers in companies with nominating committee, etc.) to entrust business execution. In doing so, directors steer

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executive officers to the management in line with shareholders’ interests. That is governance by board of directors, a substitution for governance by shareholders.

To ensure the effective governance by board of directors, those who are independent from executive officers and other stakeholders are selected as independent directors, who are the sole constituent of nominating committee, compensation committee and audit and supervisory committee. The nominating committee determines candidates of directors to submit to the shareholders' meeting. It plays an important role of choosing the competent directors, who as members of board of directors select (and dismiss) executive officers. The compensation committee sets up performance-linked incentives to provide an incentive for good management to the CEO and other executive officers selected by the board. The audit and supervisory committee checks the independence of internal and external auditors to ensure impartial and effective management.

This best practice of separating governance and management by promoting good use of independent directors has spread to the world in the last quarter century. Although directors, whose duty is to monitor executive officers, used to simultaneously serve as executive officers all over the world, it is now the global understanding that directors should be separate from executive officers in order to survive fierce competitive environments of globalization and innovation. Under this model of separation, board of directors should be centered on independent directors and focus on governance to bring about good management from executive officers, who are selected by board of directors and entrusted with management. Executives establish the management system under the governance by board of directors to pursue profit through business operations and then distribute the profit to shareholders.

3.2 Contents and categorization of questions

The current best practice in corporate governance can be characterized by (1) board of directors where outsiders play a vital role as independent directors, (2) separation of directors and executive officers, (3) nomination, compensation, and audit functions exercised by the board of directors to supervise executive officers, and (4) transparency in management.

Based on such a model, JCGIndex Survey’s questions are comprised of the following 6 parts:

Part I Performance targets, leadership of CEO 9 questions
Part II Corporate governance－Directors and board of directors－ 34 questions
Part III Management system－Execution, evaluation and compensation－ 12 questions
Part IV Management of consolidated subsidiaries 9 questions
Part V Communication with shareholders 11 questions
Part VI Officers’ Compensation Survey 11 questions

Part VI aims at grasping the current situation of officers’ compensation in Japanese companies, and is not incorporated into JCGIndex. The remaining 75 questions from Part I to Part V are recategorized into 4 categories to calculate sub-scores for each category. Each category represents the following perspective:

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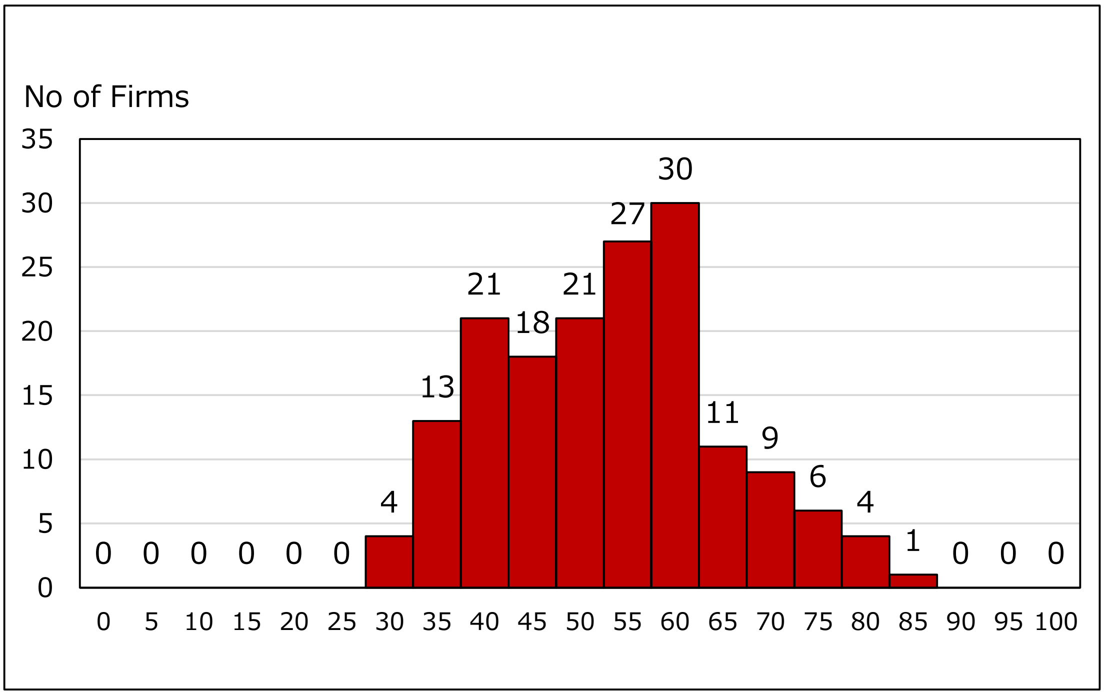
Category I Performance targets and structure of responsibilities of management
Based on Part I
Category II Functions and composition of board of directors
Based on Part II
Category III Executive management structure of top management
Based on Part III and Part IV
Category IV Communication with shareholders and transparency
Based on Part V

Categories I and II are related to corporate governance system, and III and IV are about corporate management system. Although it is possible to evaluate the corporate governance through Categories I and II alone, Categories III and IV are incorporated into JCGIndex, based on the belief that good management system is established under the good governance system.

4. Distribution of JCGIndex

The distribution of JCGIndex for the 165 companies that responded to our survey in 2019 is as the graph in the below shows. The mean JCGIndex was 50.5, and the standard deviation was 11.5.

Table: **Distribution of JCGIndex**



Mean：50.48　Standard Deviation：11.93

It is impossible to compare this year's results to previous results because we have made drastic changes in questions for Phase II. For the trend of the distribution of JCGIndex in the surveys conducted in Phase I, see the report for the 16th survey (2017).

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5. Sub-scores and achievement rates by category

To clarify the companies' performance for each category having different weight, the table below converts the mean figure into achievement rate in percentage.

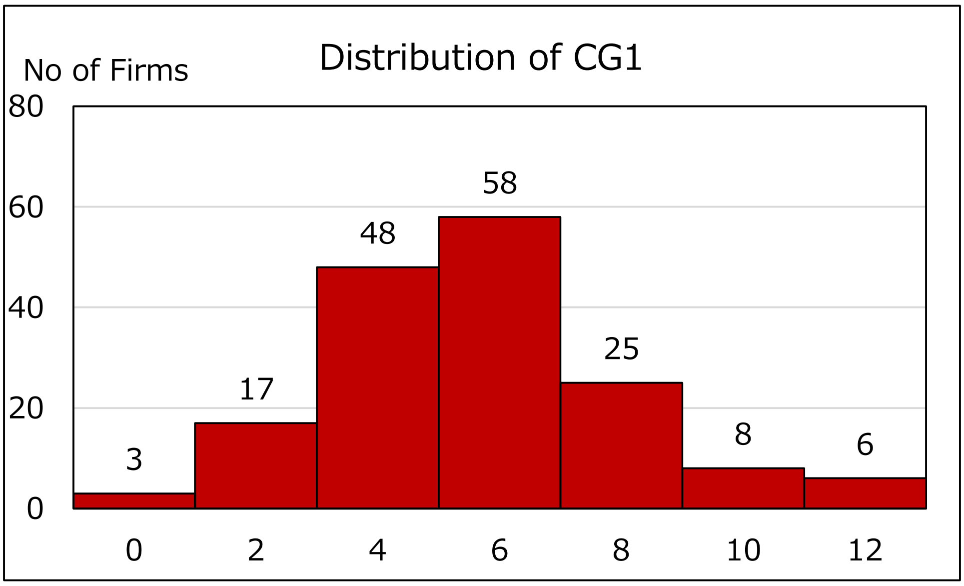
Table: **Sub-scores and achievement rates by category**

Category		Weight (A)	Mean (B)	Achievement rate (B) / (A)
I	Performance targets and structure of responsibilities of management	13.6	4.66	34.6%
II	Functions and composition of board of directors	44.8	20.22	45.1%
III	Executive management structure of top management	26.5	15.73	59.2%
IV	Communication with shareholders and transparency	15.1	9.86	65.6%
JCGIndex		100	50.48	50.5%

6. Distribution of sub-scores by category

Below are tables for distribution of sub-scores by category. CG1, CG2, CG3 and CG4 stand for sub-scores for each category. These four constitute the JCGIndex.

Category I: Performance targets and structure of responsibilities of management



Mean：4.66　Standard Deviation：2.31

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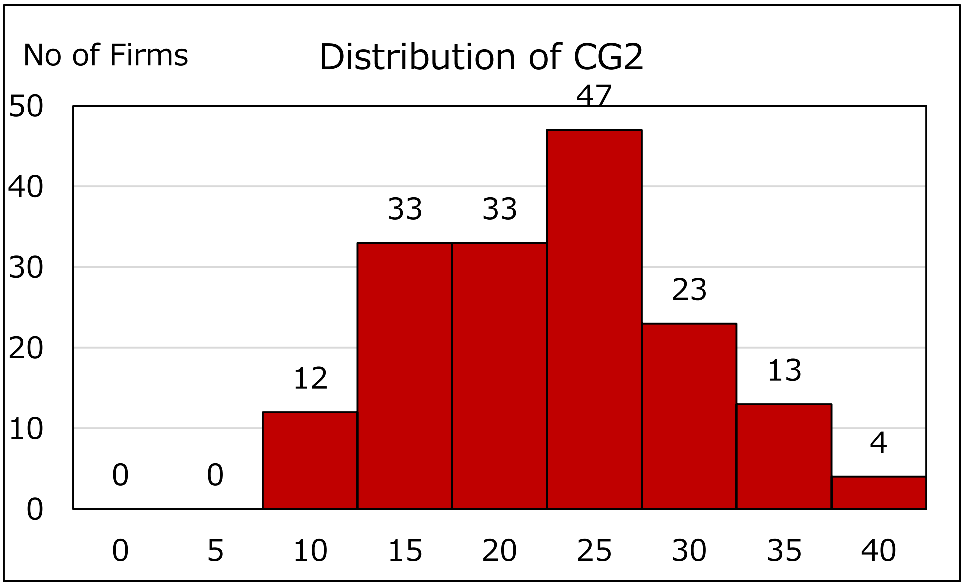
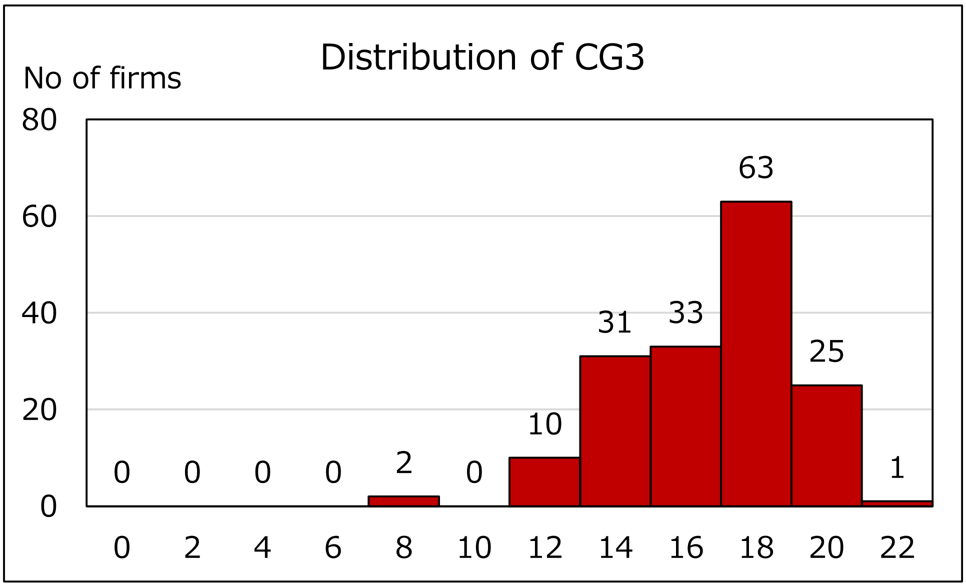
Category II: Functions and composition of board of directors



Mean：20.22 Standard Deviation：7.16

Category III: Executive management structure of top management



Mean：15.73 Standard Deviation：2.41

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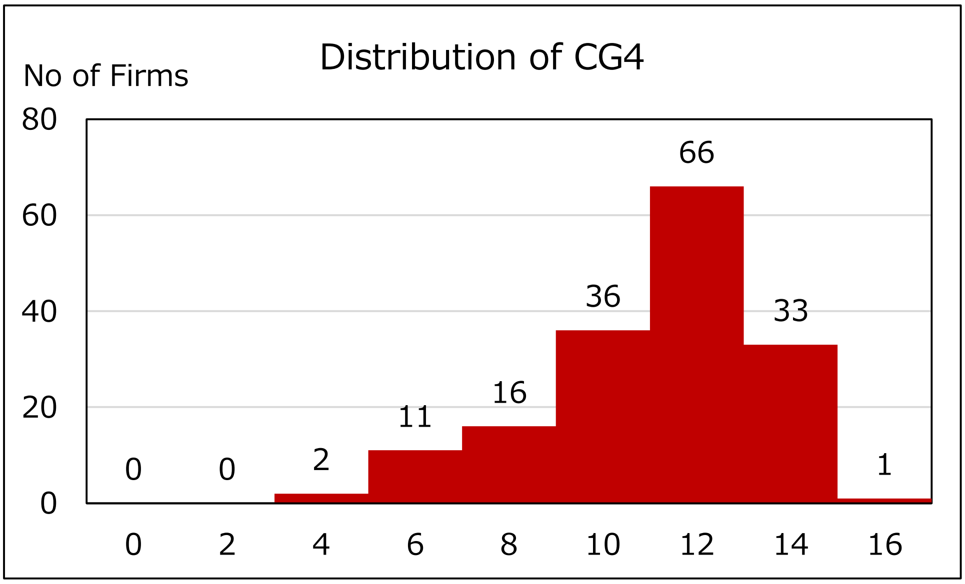
Category IV: Communication with shareholders and transparency



Mean：9.86 Standard Deviation：2.32

7. Descriptive statistics values of JCGIndex and sub-scores

Descriptive statistics values of sub-scores by category and JCGIndex are as follows.

Table: **Descriptive statistics values of sub-scores by category and JCGIndex**

	mean	standard error	median	mode	minimum	maximum	standard deviation
JCGIndex	50.48	0.926	51.4	46.2	26.3	80.2	11.90
Category I	4.66	0.180	4.3	3.3	0	11.5	2.31
Category II	20.22	0.557	20.5	21.2	6.2	37.7	7.16
Category III	15.73	0.188	16.2	17.2	7.0	20.5	2.41
Category IV	9.86	0.181	10.0	10.0	2.9	45.1	2.32

The table below shows the coefficients of variation (=standard deviation/mean) for each sub-score by category and JCGIndex.

Table: **Coefficients of variation of sub-scores by category and JCGIndex**

	Category I	Category II	Category III	Category IV	JCGIndex
Coefficient of variation	0.496	0.354	0.153	0.235	0.236

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The coefficients of variation for Categories I and II for governance evaluation are larger than those for Categories III and IV for management evaluation, meaning that the level of governance varies among companies compared to the level of management. In the future, we might see corporate governance improve more rapidly than corporate management in Japan.

8. Correlations among sub-scores and JCGIndex

The table below shows correlation coefficients between categories and between a category and JCGIndex. Not only are the correlations among categories below 0.5 (except for the correlation between Category I and Category II and the correlation between Category II and Category III) but also every category shows higher correlation with JCGIndex than with any other category, which means that each category does not overlap with others greatly and rather covers distinctive factors. It is therefore meaningful to calculate JCGIndex with these four categories by setting two separate categories for both governance and management as the result of governance.

During Phase I, scores for Categories I and II tended to be low while scores for Categories III and IV tended to be relatively high. For the trend of each Category's score, see the report for the 16th survey (2017).

Table: **Correlations among sub-scores and JCGIndex**

	Category I	Category II	Category III	Category IV	JCGIndex
Category I	1.0000				
Category II	0.6302	1.0000			
Category III	0.4676	0.6182	1.0000		
Category IV	0.4706	0.4947	0.4355	1.0000	
JCGIndex	0.7600	0.9459	0.7503	0.6723	1.0000

Category II has the highest figure for correlation among the four Categories, which may be because the category occupies the most weight. (JCGIndex is merely the sum of the sub-scores for the four categories.) Still, since the correlations among categories are low as the table above shows, every category represents distinctive factors of corporate governance.

9. High JCGIndex companies and low JCGIndex companies

The mean of JCGIndex is 50.48, and the standard deviation of JCGIndex is 11.90 for 2019. Mean plus a standard deviation equals to 62.38 and mean minus a standard deviation equals to 38.58. From these calculations, we define JCGIndex of 62.4 or more to be high JCGIndex, and JCGIndex of 38.58 or less to be low JCGIndex. With the actual number of high JCGIndex companies being 24 (14.5% of the total) and low JCGIndex companies 28 (17.0% of the total), the distribution of JCGIndex is close to normal distribution (in a normal distribution, companies above/below a standard deviation would constitute approximately 15.9% for each).

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The table below exhibits the sub-scores by category and JCGIndex of the high and low JCGIndex companies. Figures for the remaining intermediate JCGIndex companies are presented just for reference.

To clarify the difference of sub-scores by category and JCGIndex between high and low JCGIndex companies, the ratios of high JCGIndex companies' scores to those of low JCGIndex companies are presented at the bottom of the table. High JCGIndex companies achieve more than twice as much JCGIndex as low JCGIndex companies.

Table: **High JCGIndex companies and low JCGIndex companies**

	Category				JCGIndex
	I	II	III	IV	
High JCGIndex companies (24)	8.33	31.28	18.03	12.46	70.10
Intermediate JCGIndex companies (131)	4.40	20.13	16.09	9.89	50.51
Low JCGIndex companies (28)	2.58	11.10	12.33	7.53	33.54
Ratio of difference between high and low JCGIndex companies	3.23	2.82	1.46	1.65	2.09

The table above presents, however, that the ratio of difference between high and low JCGIndex companies is more than twice for Categories I and II for governance evaluation, but less than twice for Categories III and IV for management evaluation. This implies that a company's corporate governance is well characterized by Categories I and II, and thus is consistent with the finding in Section 7 that the level of governance varies among companies compared to the level of management.

10. Conclusion

This report reorganized the questionnaire results of the 17th Corporate Governance Survey (the first Phase II Survey) relevant to JCGIndex (i.e. excluding Officers' Compensation Survey) into the basic statistics. The overall results and analysis are to be published later.

Although it is ideal that each company's JCGIndex is shared by society, the JCGR only discloses JCGIndex of the companies that have approved the disclosure of their JCGIndex, conceding that it might be inconvenient for some companies to disclose their JCGIndex. The list of the companies with high JCGIndex and their JCGIndex is added to this report. For the list of all companies that responded to the survey and companies that fall in the upper half of the JCGIndex rankings, see List of responding firms and List of companies in the upper half.

※ The Corporate Governance Survey has been funded by the University of Michigan Ross School of Business Mitsui Life Financial Research Center since 2008.

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【Appendix】 Companies with high JCGIndex in 2019（88 companies）

Rank	JCGIndex	Company
1	80.2	Sony Corporation
2	79.2	Hitachi, Ltd.
3	78.0	Eisai Co., Ltd.
4	75.8	Konica Minolta Japan, Inc.
5	75.2	Yamato Holdings Co., Ltd.
6	74.3	Ebara Corporation
7	72.7	Nippon Sheet Glass Co., Ltd.
8	72.6	Ichiyoshi Securities Co., Ltd.
9	71.3	Terumo Corporation
10	70.2	Omron Corporation
11	70.2	Yokogawa Electric Corporation
12	69.6	Kobe Steel, Ltd.
13	69.6	Resona Holdings, Inc.
14	69.2	J. FRONT RETAILING Co., Ltd.
15	68.6	NSK Ltd.
16	67.1	JVCKENWOOD Corporation
17	66.4	Sangetsu Corporation
18	66.1	*（1 company）
19	66.0	Seven & i Holdings Co., Ltd.
20	65.1	PeptiDream Inc.
21	64.8	Santen Pharmaceutical Co., Ltd.
22	64.3	SWCC Showa Holdings Co., Ltd.
21	63.3	Lawson, Inc.
24	62.7	*（1 company）
25	61.8	MOS FOOD SERVICES, INC.
26	61.7	BIC CAMERA INC.
27	61.7	ROHM Co., Ltd.
28	61.5	SHIONOGI & CO., LTD.
29	61.4	ANA HOLDINGS INC.
30	61.3	Nissin Food Products Co., Ltd.
31	60.7	* (1 company)
32	60.0	ALPS ALPINE CO., LTD.
33	58.8	Hitachi Capital Corporation
34	58.5	* (1 company)
35	58.4	Mitsubishi Chemical Holdings Corporation
36	58.0	Kao Corporation
37	57.7	DAI-DAN Co., Ltd.
38	57.4	* (1 company)
39	57.2	Nippon Suisan Kaisha, Ltd.
39	57.2	TODA CORPORATION
41	57.1	Shiseido Company, Limited
41	57.1	Mandom Corporation

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41	57.1	IHI Corporation
41	57.1	* (1 company)
45	56.8	Tokyo Electron Limited
45	56.8	* (1 company)
47	56.7	Takasago Thermal Engineering Co.,
47	56.7	FUJITEC CO., LTD.
47	56.7	* (1 company)
50	56.2	Sumitomo Heavy Industries, Ltd.
51	56.1	** (2 companies)
53	55.8	Calbee, Inc.-
53	55.8	Bando Chemical Industries, Ltd.
53	55.8	* (1 company)
56	55.7	* (1 company)
57	55.5	IBIDEN CO., LTD.
57	55.5	Mitsubishi Heavy Industries, Ltd.
57	55.5	** (2 companies)
61	55.1	Mitsubishi Tanabe Pharma Corporation
62	54.9	KITZ CORPORATION
63	54.5	* (1 company)
64	54.4	Sanki Engineering Co., Ltd
64	54.4	* (1 company)
66	54.2	HISAMITSU PHARMACEUTICAL CO., INC.
66	54.2	Miraca Holdings Inc.
66	54.2	SBI
66	54.2	* (1 company)
70	53.9	Kawasaki Heavy Industries, LTD.
71	53.7	SENSHU ELECTRIC CO., LTD.
72	53.5	TANABE MANAGEMENT CONSULTING CO., LTD.
73	53.4	SUMITOMO MITSUI CONSTRUCTION CO., LTD.
73	53.4	Infocom Corporation
73	53.4	Lion Corporation
76	52.8	JBCC Holdings Inc.
77	52.7	HONDA TSUSHIN KOGYO CO., LTD.
78	52.2	Meiko Network Japan Co., Ltd.
78	52.2	TOPPAN FORMS CO., LTD.
78	52.2	* (1 company)
81	51.8	* (1 company)
82	51.5	Advantest Corporation
83	51.4	Fujicco Co., Ltd.
84	50.6	ARTNER CO., LTD.
85	50.5	YAMASHITA HEALTH CARE HOLDINGS, INC.
86	50.4	* (1 company)
87	50.2	Matsumotokiyoshi Holdings Co., Ltd.
87	50.2	* (1 company)

※ An asterisk represents a company that declined to disclose its name.

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