
Evolution of General Shareholders' Meetings in Japan

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I. Introduction

Annual general meetings of shareholders (AGMs) in Japan have undergone a transformation over the past ten years. In the past, most of these meetings were rubber-stamp affairs with almost no opportunity for attendees to ask questions, and general shareholders did not give the AGM much thought. With shareholding racketeers (called *sokaiya* in Japan) having become less active, however, meetings more open to the shareholders themselves have already become the norm. This trend toward more open AGMs has stoked greater interest in shareholder voting, and AGMs have begun to function as effective decision-making bodies. In this report, we look back at how AGMs have changed over the past decade, and discuss the challenges that lie ahead.

II. From rubber-stamp meetings to meetings that are open to shareholders

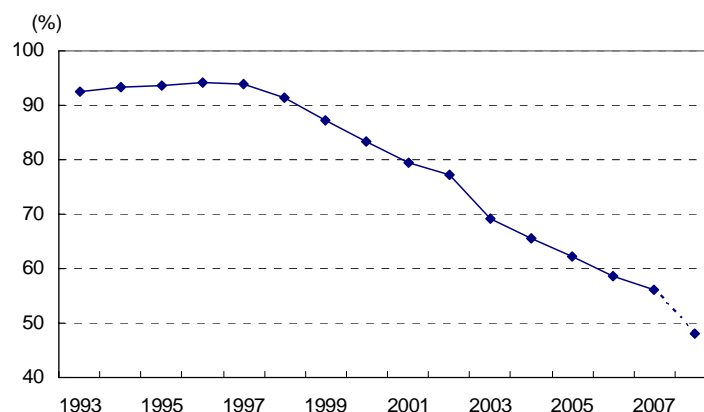
1. AGMs open to shareholders

We define an AGM open to shareholders as a meeting that it is easy for regular shareholders to participate in. In the past, many companies held their AGMs on the last Thursday in June to make it harder for the *sokaiya* to attend multiple AGMs, but meeting schedules have gradually become less concentrated. According to the White Paper on Shareholders' Meetings published by the Commercial Law Center, 93.8% of all listed companies (1,807 of 1,927 companies) held their AGM on the same day in June 1997, but this number had declined to only 56.2% (1,138 of 2,025 companies) in June 2007. According to data compiled by Nihon Keizai Shimbun Sha, that percentage dropped below 50% for the first time in 2008, down to approximately 48% (Figure 1)¹. Although about half of the companies with a fiscal year ending in March

¹ Kabunushi Sokai -- Shuchuudo Gowari Shitawamaru (Same-day general shareholder meetings drop below 50% of total), 8 June 2008 edition of the Nihon Keizai Shimbun.

still hold their annual meetings on the same day, it is now easier than it was before for shareholders to participate.

Figure1: Percentage of annual meetings held on the same day



Note: Figures are for companies with a fiscal year ending in March. Data through 2007 are from the White Paper on Shareholder Meetings, but the 2008 data are from an article in the Nikkei Shimbun, and thus lack continuity with the data up until 2007

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center, and based also on a Nihon Keizai Shimbun article

Secondly, the annual meeting has become a platform for investor relations (IR). At many companies, management now uses visual aids, such as PowerPoint presentations and videos, when explaining earnings and other details to shareholders, and executives have become more receptive to fielding questions. A growing number of companies are now encouraging individual investors to attend their shareholder meetings by providing samples of their products, holding concerts (in the case of entertainment companies) or other events in conjunction with the meeting, or holding roundtable discussions with shareholders following the annual meeting as a forum for shareholders to share their opinions.

Third, the AGMs are now designed so as to make it easier for nonresident shareholders to vote. Nonresident investors have long pointed out that, in addition to most AGMs being scheduled in late June, the short period between the time the notices are sent out and the day of the meeting does not leave enough time to closely review the proposals. A growing number of companies have responded to this complaint by sending meeting notices out early². After the commercial code was revised in 2001, there was an increase, albeit gradual, in the number of companies

² According to the White Paper on Shareholders' Meetings, 35.5% of companies surveyed in 2007 sent out annual meeting invitations early as a way to increase shareholder voting and the return of proxy authorizations. That number was only 7.4% in the 1999 survey.

sending out notices and conducting shareholder votes electronically³, and this is making it easier for nonresident shareholders to vote (Figure 2)⁴.

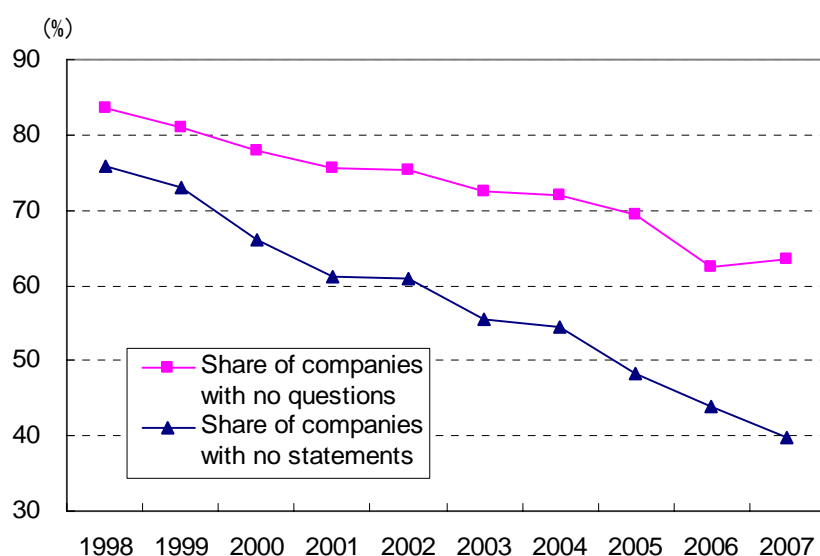
Figure2: Measures to encourage nonresident shareholders to exercise their voting rights

	(%)							
	2000	2001	2002	2003	2004	2005	2006	2007
Online meeting notices and proxy voting	-	-	0.9	2.6	4.4	6.1	8.8	11.1
Meeting notice in English on Website	-	3.5	4.8	5.9	7.7	8.9	8.7	9.9
Create and send out meeting notices in English	5.8	5.8	6.1	7.0	7.2	7.8	8.7	9.1
Outsource research on shareholder details	2.7	3.4	3.8	3.7	4.3	6.0	6.8	9.0
Outsource promotion of proxy voting	2.3	2.3	3.0	3.1	3.3	3.4	3.4	3.8
Not doing anything special	89.5	87.7	87.9	85.6	83.2	80.2	80.3	78.4

Note: Survey is of domestic companies listed on one of Japan's five stock markets, including the TSE, OSE, or NSE. Multiple answers were allowed

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center

Figure3: Whether there were shareholder statements/questions at annual meetings



Note: Survey is of domestic companies listed on one of Japan's five stock markets, including the TSE, OSE, or NSE

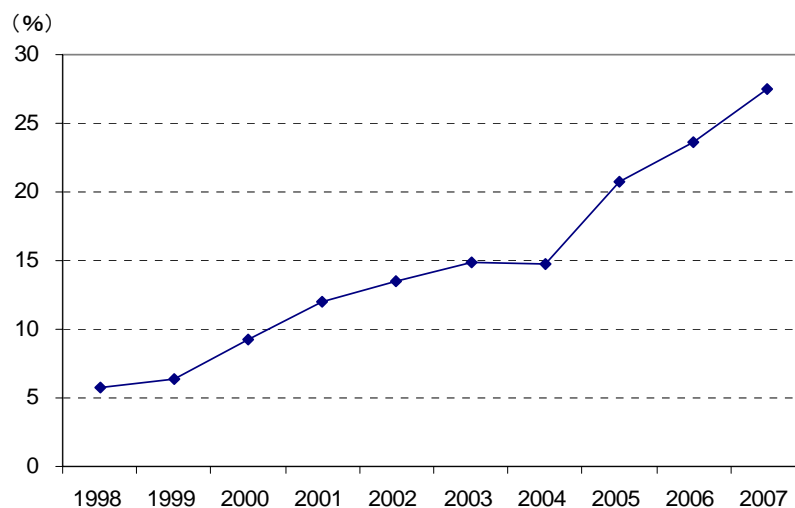
Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center

³ The White Paper on Shareholders' Meetings notes that although only 2.3% of companies answering the survey sent out annual meeting notices electronically, the number of companies answering that they used electronic proxy voting had increased to 383 (19.6% of the companies that responded to the survey) in 2007.

⁴ An electronic proxy voting platform for institutional investors operated by Investor Communications Japan (ICJ), a joint venture established by the Tokyo Stock Exchange, the Japan Security Dealers Association, and US-based ADP (now Broadridge Financial Solutions).

The opening of AGMs to regular shareholders resulted in an increase in both meeting attendance and the number of shareholder statements or questions, particularly from individual investors (Figure 3), and annual meetings are now taking longer to complete (Figure 4).

**Figure4: Time required to hold annual meeting
(proportion of companies with meetings lasting at least 60 minutes)**



Note: Survey is of domestic companies listed on one of Japan's five stock markets, including the TSE, OSE, or NSE

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center

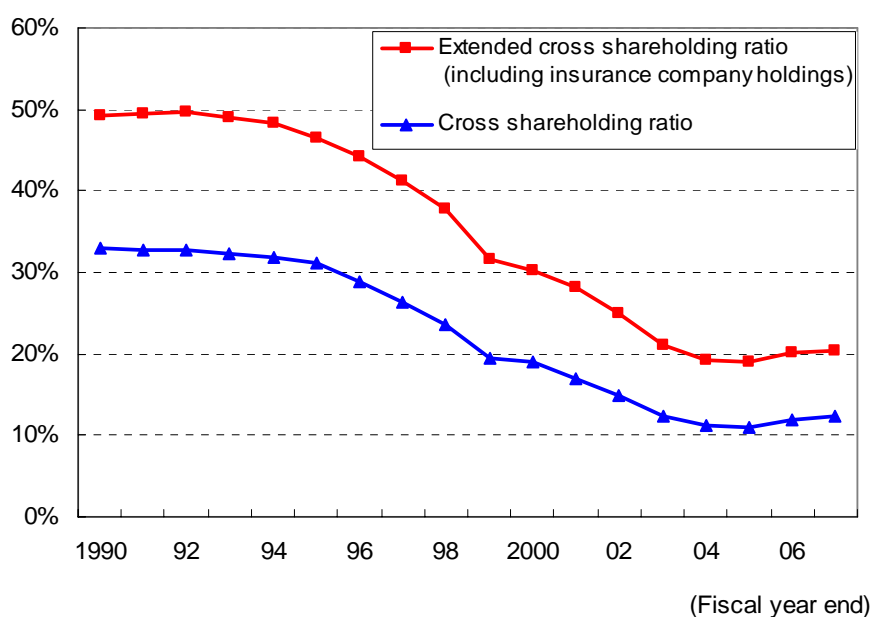
2. Why AGMs have become more open

Why have AGMs been opened to shareholders? The first likely reason is that the *sokaiya* have become less active. There was a rapid decline in *sokaiya* activity toward the end of the 1990s as a result of strengthened oversight by regulators, efforts by companies to distance themselves from the racketeers, and the establishment of new laws, and stronger penalties related to demands for protection money (with 1997 revisions to the Commercial Code). This reduced the need for companies to hold their annual meetings on the same day⁵. Measures taken by companies to combat the *sokaiya* were affected by an Osaka District Court decision in March 1998 that criticized heavy-handed tactics taken by Sumitomo in a shareholder lawsuit demanding the overturning of an AGM resolution. Following that court decision, there has been a decrease both in the intimidation of regular shareholders by companies and in annual meeting participation by employee shareholders.

⁵ The *Enforcement Regulations for the Company Act* further encouraged a move away from same-day annual meetings by requiring companies to disclose their reasons for holding their annual shareholders meeting on the same day as other companies.

Second, as companies unwind their cross shareholdings, a growing number of companies have been courting individual shareholders as a new source of stable shareholders. Cross shareholdings have been in a declining trend since the mid-1990s, and accounted for only 11.1% of outstanding shares at end-FY2005 (Figure 5). There are several reasons for this unwinding of cross shareholdings, including 1) the introduction of mark-to-market accounting in 2000, which required companies to carry cross-held shares on the balance sheet at their market value each fiscal period, thereby necessitating unrealized losses when the share price declined⁶, 2) the selling of cross-held shares by banks weakened by nonperforming loan disposals, and 3) the bank mergers that resulted in the new megabanks going over the 5% rule⁷ and having to sell off their surplus shares. Consequently, many Japanese companies have looked to individual shareholders as a new source of “stable” shareholders. To increase the number of their individual shareholders, a growing number of companies performed stock splits to make it easier to invest in their shares, positioned their annual meetings as an investor relations tool, and encouraged greater AGM attendance by individual shareholders.

Figure5: Cross shareholding ratios



Source: Nomura Securities Financial & Economic Research Center

Third, the spate of corporate scandals and growing trend toward mergers has increased calls for greater transparency at annual meetings. In the US, major accounting scandals at Enron in 2001 and WorldCom in 2002 led to the Sarbanes-

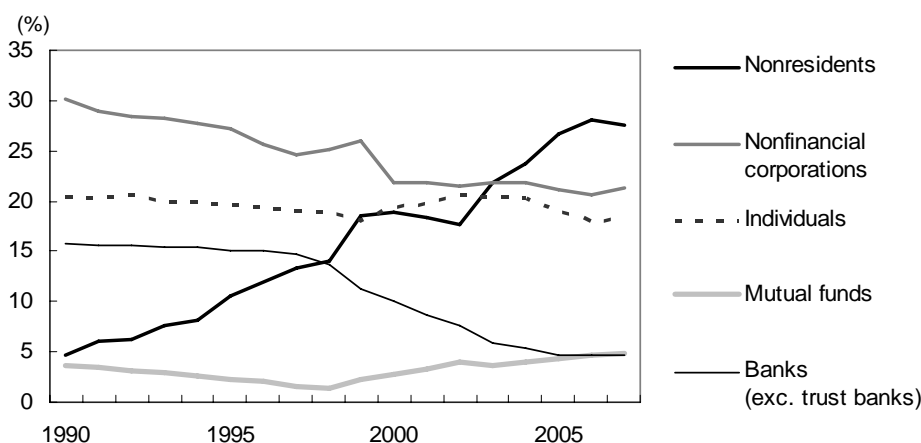
⁶ Valuation gains from changes in market value are directly recorded on the net assets portion of the balance sheet as valuation differences on other securities (i.e., added directly to net assets).

⁷ Article 3-1 of the *Banking Act* prohibits banks and their subsidiaries from acquiring 5% or more of the voting rights of a Japanese company.

Oxley Act (SOX), an attempt to strengthen corporate governance. The impact of SOX, together with a series of corporate scandals starting in the early 2000s, increased investor demands for stronger corporate governance in Japan, as well. Consequently, the annual general meetings were held to empower shareholders with a corporate governance role, i.e., to provide a forum for shareholders to “check and balance” management once a year.

Fourth, to meet quorums and to address other issues, companies with a high percentage of nonresident shareholders implemented a number of different measures to encourage proxy voting by nonresident shareholders. The breakdown of shareholders by type at Japanese companies has shown, with the exception of one period, a consistent increase over the past 20 years in the percentage of shares held by nonresident investors, which reached 28% in 2006 (Figure 6). With ownership by nonfinancial corporations and the banks declining and ownership by domestic individual shareholders holding steady, it is clearly nonresident investors and domestic institutional investors that are absorbing the cross-held shares being sold⁸. There are some companies where nonresident shareholders own more than 50% of the shares outstanding (Figure 7). Some companies with a high percentage of nonresident shareholders are now finding it difficult to meet the quorum for special resolutions at general shareholders’ meetings (which is a majority of general shareholder votes) if its nonresident shareholders do not vote⁹, and these companies have responded by implementing measures to make it easier for nonresidents to vote. Some companies have even begun to hire solicitors, which are service providers that specialize in such tasks as surveying nonresident shareholders and encouraging proxy voting.

Figure6: Share ownership by investor category



Source: Nomura Institute of Capital Markets Research, based on the FY2007 Shareownership Survey, taken by the domestic securities exchanges

⁸ In many cases, the unwinding of cross-held shares has been absorbed by share buybacks.

⁹ There are now fewer companies that have difficulty achieving a quorum because of a 2002 revision to the *Commercial Code*, which allowed for lowering, via stipulation in the Articles of Incorporation, the quorum for special resolutions at the general shareholders’ meeting to one-third of the general shareholder voting rights.

Figure7: Companies with a high percentage of nonresident investor shareholders

Rank	Company	Sector	Nonresident shareholder ratio (%)	Market cap ¥ billions
1	Orix	Miscellaneous finance	66.03	1,528.8
2	Yamada Denki	Retail	59.10	709.5
3	Nitto Denko	Chemicals	55.94	540.4
4	eAccess	Information and Communications	55.47	79.5
5	Meitec	Information and Communications	55.36	94.1
6	Hoya	Precision instruments	51.91	970.1
7	Sony	Electronics	50.73	4,138.7
8	Mitsui Fudosan	Real estate	50.52	2,177.1
9	Misumi Group	Wholesale	50.49	182.0
10	Credit Saison	Miscellaneous finance	50.31	415.6
11	Rohm	Electronics	50.29	734.2
12	Aderans Holdings	Other products	49.96	80.0
13	SMC	Machinery	48.53	776.2
14	Kenedix	Services	48.50	50.1
15	Leopalace21	Real estate	48.28	232.8
16	Konica Minolta Holdings	Electronics	46.82	944.2
17	Astellas Pharma	Pharmaceuticals	46.66	2,363.6
18	FujiFilm Holdings	Chemicals	46.59	1,749.7
19	Hirose Electric	Electronics	45.57	411.0
20	Risa Partners	Real estate	45.47	44.3

Note: (1) Numbers current as of end-July 2008. Based on stocks in the TOPIX

(2) Excludes ownership by operational companies and private equity

Source: Nomura Institute of Capital Markets Research, based on Bloomberg data

III. AGMs are starting to function as effective decision-making bodies

1. AGMs that were by nature rubber-stamp affairs

Although the general shareholders' meeting is said to be a company's highest-level decision-making body, the authority of AGMs for companies with a board of directors is in principle limited to those matters set forth in the *Company Act*, which are (1) matters related to the appointment and removal of directors and auditors for the organization; (2) matters related to fundamental changes in the corporation (including changes in the articles of incorporation, a corporate merger or split, and dissolution of the company), (3) matters of important interest to the shareholders (including reverse stock splits and the distribution of surplus funds), and (4) matters at a high risk of harming shareholders if left up to the directors (including decisions on director compensation)¹⁰. Nevertheless, although limited, all of these matters are at the bedrock of the company's management, including director appointments, merger approvals, and changes to the articles of incorporation, and the AGM still retains important legal authority. That said, the decisions made at the annual meetings have typically been formalities, with shareholders rarely objecting to management

¹⁰ Quoted from a passage starting on page 154 of *The Company Act, Ninth Edition*, written by Hideki Kanda and published by Koubundou in 2007.

proposals. In that sense, AGM voting has by nature been largely ceremonial. For the reasons outlined below, however, around the year 2000 shareholder voting rights started attracting more attention and AGMs have begun to function as effective decision-making bodies.

2. Reasons for increased interest in shareholder voting

Increased attention can be attributed to greater awareness among institutional investors of their fiduciary responsibilities and to their establishment of voting guidelines. The Pension Fund Association (PFA) put together a handbook on fiduciary responsibilities (investment institution edition) in 2000, in which it noted the need for investment institutions to properly exercise the voting rights of the stocks included in pension assets, and the desirability of the pension funds (trustors) monitoring voting arrangements and the votes cast¹¹. In 2001, the PFA compiled a set of practical guidelines on exercising shareholder voting rights for investment institutions acting as trustees. Based on this, trust banks, life insurers, and other institutional investors in Japan established internal mechanisms, and put together their own guidelines, for shareholder voting. This resulted in Japan's institutional investors also casting votes against management proposals when required by the guidelines. The PFA began directly investing in equities in 2002, compiled a booklet on corporate governance principles and standards for exercising shareholder voting rights in 2003, and based on those, has often voted against management at general shareholders' meetings.

Second was the emergence of activist funds, which are investment vehicles that, on the basis of their ownership stakes, make a variety of demands of, and proposals to, the companies they invest in, with the goal of increasing those companies' enterprise value. In the US, activist hedge funds and hedge funds with an event-driven strategy¹² are often put in this category¹³. The Murakami Fund (M&A Consulting), led by the former MITI bureaucrat Yoshiaki Murakami, initiated the first activist move on a Japanese company by an investment fund in 2000 with its attempt at a hostile takeover of Shoei. These activist funds have made various proposals and demands of the companies they invest in through proxy battles and shareholder proposals at the general meeting. Also, although not activist funds, there were some nonresident institutional investors, fed up with the persistently weak earnings and share price performance of Japanese companies, that began using their voting rights to request dividend increases and make other shareholder proposals.

Third is the emergence of companies in Japan that offer assistance with the proxy voting process, a service, originally conceived in the US, that assists institutional

¹¹ For a more detailed explanation of the handbook on fiduciary responsibilities, see Motomi Hashimoto, *The Fiduciary Responsibility Guidelines For Asset Management Companies - Deliberations and Findings of the Fiduciary Responsibility Working Group -*, *Capital Research Journal*, Autumn 2000 issue.

¹² A strategy of investing in opportunities created by such corporate events as spin-offs, M&A, company reorganizations, recapitalizations, and share buybacks.

¹³ For more on activist funds in the US, see Masanobu Iwatani, *Beikoku Akutibesto Fando no Jittai to Shihon Shijou ni okeru Yakuwari (US Activist Funds and their Role in Capital Markets)*, *Capital Market Quarterly*, Fall 2007 issue (in Japanese).

investors in deciding, based on certain criteria, whether to vote for or against the numerous proposals made by the companies they invest in. Institutional Shareholder Services (ISS)¹⁴, the largest provider of such services in the US, began covering Japanese stocks in 1993, and fully launched its Japan business in 2001 when it established an office in Tokyo. In 2004, IRRC (now a subsidiary of ISS), and in 2006, Japan Proxy Governance (a subsidiary of US-based FOLIOfn) and US-based Glass Lewis, all established offices in Japan. Although there are differences among these advisory service providers in their specific analytic methods, they all recommend voting against takeover defenses and other proposed changes to articles of incorporation that they deem at risk of harming shareholder interests¹⁵. With the number of resolutions aimed at defending against takeovers increasing since 2005, the impact that these advisors have had on the decisions by domestic and overseas institutional investors on whether to support such proposals has attracted a lot of attention. The criteria determining support for takeover defenses appears to have become stricter in the 2008 season for general shareholder meetings, when ISS and Glass Lewis, which used to allow some takeover defenses under certain conditions, both voted against nearly every takeover defense that was proposed¹⁶.

3. Rise of participation and increase in opposition votes

Growing awareness of proxy voting and more meaningful general shareholders' meetings led to an increase in vote participation rates and in the number of "no" votes cast. Regarding the former, only 14.6% of companies answered that at least 30% of the ballots or proxy authorizations sent out were returned in 1998, but this had risen to 55.6% by 2007 (Figure 8). This suggests that individual investors are becoming more interested in shareholder voting.

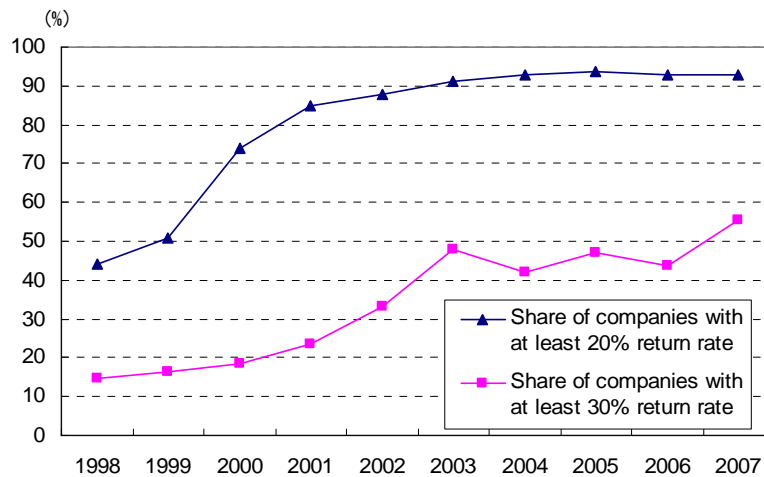
As the probability of receiving "no" votes at general meetings increased, management has been forced to become more conscious of voting results. The percentage of companies answering that institutional shareholders had voted against resolutions increased from 17.5% in 1998 to 59.3% in 2007 (Figure 9), and among companies with at least ¥100 billion in capital, that percentage in 2007 was 89.9%. As a result of domestic and overseas institutional investors closely examining each resolution based on their proxy guidelines, "no" votes are no longer an exception.

¹⁴ ISS was acquired by Risk Metrics and made a subsidiary in 2007.

¹⁵ Recently a growing number of companies have been briefing these advisory firms prior to making proposals, since the advisory firms' recommendations are based on the situation at each company and the specifics of each proposal, rather than on a checklist of criteria outlined in a rigid set of rules.

¹⁶ Giketsuken Ohte Nisha, Boeisaku no Dounyuu, Taihan ni Hantai (Two leading proxy service companies mostly opposed to takeover defenses), Nihon Keizai Shimbun, 25 June 2008 edition (in Japanese).

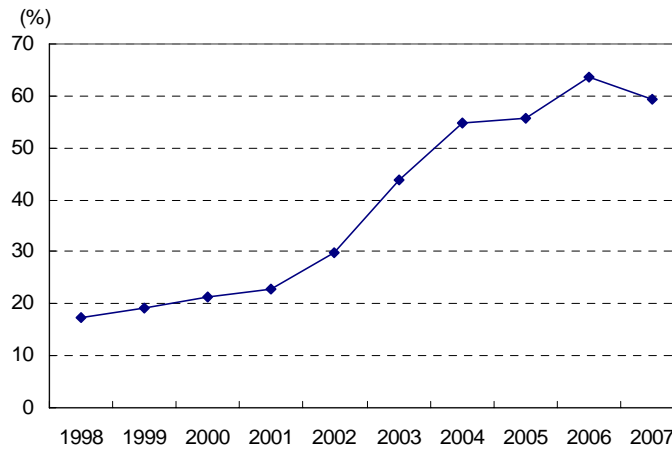
Figure8: Percentage of ballots or proxy cards sent out that are returned



Note: Survey is of domestic companies listed on one of Japan's five stock markets, including the TSE, OSE, or NSE

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center

Figure9: Percentage of companies answering that institutional investors had voted "no"



Note: Survey is of domestic companies listed on one of Japan's five stock markets, including the TSE, OSE, or NSE

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center

In some cases, management proposals are rejected (Figure 10). The rejection by Tokyo Kohtetsu of Osaka Steel's merger proposal showed that it is possible in Japan for shareholder opposition to block a merger already agreed upon by the management of both sides. In this case, Ichigo Asset Management (led by former Morgan Stanley Japan executive Scott Callon), a major shareholder with roughly a 10% stake in Tokyo Kohtetsu, launched a proxy battle based on its objections to what it deemed an unfair share exchange ratio for the merger. Ichigo Asset Management's success in obtaining the one-third of votes needed to overturn the special resolution at an extraordinary

general meeting was helped by many individual shareholders turning against the resolution, and made clear the potential impact from individual shareholders exercising their voting rights.

Figure10: Major examples of management proposals being rejected

Month/Year	Company	Company proposal and events leading to rejection
June 2005	Fanuc	Proposal to increase authorized share issuance in the articles of incorporation from 400 million to 900 million shares was rejected. The stated purpose of the change was to ensure a more flexible and dynamic capital policy, but an additional reason given by the company was to gain a wide range of options to block hostile takeover attempts. The proposal ultimately failed as a result of both domestic and nonresident institutional investors voting against it.
June 2005	Tokyo Electron	The reasons given for a proposal to increase authorized share issuance in the articles of incorporation from 300 million to 900 million shares included clear mention of a takeover defense, in addition to ensuring a more flexibility in capital policy. Institutional investors rejected the proposal out of concern that it would dilute the value of their shares.
June 2005	Yokogawa Electric	The reason given for a proposal to increase authorized share issuance in the articles of incorporation from 480 million to 1 billion shares was to strengthen the financial strategy, and it was noted that it was not anticipated to be for a takeover defense. The proposal was narrowly defeated.
June 2006	Nintendo	A proposal to change the articles of incorporation so as to give the board of directors the authority to dispose of surplus funds was rejected. The company considered allowing a quarterly dividend, with the basic principle being to distribute as profits the higher of either 50% of net profit or 30% of operating profit, but nonresident investors opposed the idea out of concern that it would give the board of directors too much power.
June 2006	ARRK	A proposal to change the articles of incorporation so as to set an upper limit on the liability of directors or auditors in the event of a shareholder class action.
June 2006	Japan Asia Investment	A proposal to change the articles of incorporation so as to give the board of directors the authority to dispose of surplus funds was rejected.
February 2007	Tokyo Kohtetsu	A special resolution regarding a merger with Osaka Steel was rejected. In October 2006, Tokyo Kohtetsu announced it would become a wholly owned subsidiary of Osaka Steel through an exchange of shares. The share exchange ratio was set at a level that paid almost no premium to Tokyo Kohtetsu shareholders. Ichigo Asset Management began purchasing shares in November. It had acquired an 11% stake by mid-January, and although agreeing with the deal, took the position that a 30% premium should be paid. It obtained proxy authorizations from over 500 individual investors, and secured "no" votes amounting to 42.1%.
January 2008	CFS	A proposal to merge with Ain Pharmaciez was rejected at an extraordinary shareholders' meeting. A merger with Ain Pharmaciez was announced in October 2007, but major shareholder Aeon opposed the deal and started a proxy battle. When Aeon raised its ownership stake in March 2008, the CFS president resigned.
May 2008	Aderans Holdings	A proposal to reappoint seven directors, including president Takayoshi Okamoto, was rejected as a result of opposition by Steel Partners, Dodge & Cox, and other major shareholders. Subsequently, proposals to appoint a new president as well as an outside director from Steel Partners were approved at an extraordinary shareholders' meeting in August.

Source: Nomura Institute of Capital Markets Research, based on various news reports

In addition, at an annual general shareholders' meeting held by Aderans in 2008, proposed director appointments were rejected by a vote of nine to seven. Evidently, many Aderans shareholders were unhappy with the company's persistent share price weakness caused by poor earnings, and a number of them sided with Steel Partners, the largest shareholder with a 29% stake, in its opposition to the reappointment of directors. There was ultimately a substantial change in management, with five directors, including the president and representative director, removed from the board and two new outside directors recommended by Steel Partners appointed. The actual forced removal of directors by a major shareholder at a general meeting should probably be seen as a critical event in the evolution of Japan's general shareholders' meetings.

4. Shareholder proposals from activist funds and nonresident investors

Shareholder proposals worth noting include a proposed change to the articles of incorporation (for new rules to accommodate the anti-nuclear and environmental movements) of the electric power companies by shareholders opposed to nuclear energy, and a proposal by Shareholder Ombudsman¹⁷ to Sony, Sumitomo Mitsui Banking, and other companies requiring disclosure to shareholders of the compensation to individual directors. Recently, however, some general meetings have digressed into a battle over votes between management and shareholders, and there are notable examples of shareholder proposals as well as opposition to management proposals from the activist funds (Figure 11). Companies that have actually received shareholder proposals from funds have an increased administrative burden, including providing detailed disclosures in their meeting invitations and preparing for and providing advanced briefings on said proposals to other shareholders and proxy advisory service providers like ISS.

Shareholder proposals made by funds, mostly consisting of large dividend increases and aggressive share buybacks, were covered heavily by the media, but it is unclear whether shareholder proposals will catch on as a tool for activist funds to confront management, given that, in addition to management at Japanese firms having become more defensive as a result, (1) such proposals are only coming from a limited number of investors, (2) the number of proposal declined substantially in 2008, after climbing into the double digits in 2007, and (3) all shareholder proposals have thus far been rejected. There have been instances recently where the possibility of a shareholder proposal has exerted enough subtle pressure to persuade management to propose a modest dividend increase or share buyback on its own.

¹⁷ A not-for-profit citizens' organization established in February 1996, Shareholders Ombudsman is a shareholders' advocacy group with the goal of rectifying unlawful corporate actions and promoting sound corporate behavior. Members include attorneys, CPAs, academics and other specialists, individual shareholders, and the general populace.

**Figure11: Major shareholder proposals from activist funds
and nonresident institutional investors**

Year	Company	Proposing shareholder	Share of voting rights	Proposal
2000	Shoei	M&A Consulting and others	6.4%	Appointment of one director
2002	Tokyo Style	M&A Consulting and others	11.9%	Dividend increase and share buyback
2003	Tokyo Style	M&A Consulting and others	13.8%	Appointment of two directors
2004	Tokyo Style	M&A Consulting and others	15.1%	Share buyback
2007	Aderans Holdings	Steel Partners	24.6%	Dividend increase
	Sapporo Holdings	Steel Partners	17.9%	Takeover defense nullified
	TTK	Steel Partners	6.3%	Takeover defense nullified
	Ezaki Glico	Steel Partners	16.4%	Dividend increase
	Brother Industries	Steel Partners	9.3%	Dividend increase
	Denki Kogyo	Steel Partners	10.2%	Dividend increase
	Fukuda Denshi	Steel Partners	14.1%	Dividend increase
	Inaba Denki Sangyo	Steel Partners	8.1%	Dividend increase
	Electric Power Development	The Children's Investment Fund	10.0%	Dividend increase
	Chubu Electric Power	The Children's Investment Fund	1.4%	Dividend increase
	SNT	Safeharbor Investment	7.1%	Dividend increase
	Ono Pharmaceutical	Brandes Investment Partners	0.5%	Appointment of two directors
	2008	Electric Power Development	The Children's Investment Fund	9.9%
Hibiya Engineering		Brandes Investment Partners	Over 9%	Dividend increase, share buyback, director appointment, and limit on cross shareholding

Note: Vote participation rates are at the time of the AGM

Source: Nomura Institute of Capital Markets Research, based on the White Paper on Shareholders' Meetings published by the Commercial Law Center and on newspaper articles

IV. Backlash from hostile takeover threats

Although the resurgence of proxy voting has given new life to what had been rubber-stamp general shareholders' meetings, unlike a situation in which the companies were motivated on their own to hold open meetings, the increase in "no" votes and shareholder proposals resulting from this greater focus on proxy voting has not always been welcomed by management. This, together with the hostile takeover attempts¹⁸ of listed companies that have become frequent in Japan since 2000 (Figure 12), has put management on the defensive recently, directly resulting in the adoption of takeover defenses, and indirectly resulting in a revival of cross shareholding aimed at securing stable shareholders.

¹⁸ Although not an example of a hostile takeover, the battle between Livedoor and Fuji Television Network over control of Nippon Broadcasting in 2005 also encouraged listed companies to adopt takeover defenses.

Figure12: Recent examples of hostile takeover attempts

Year	Target company	Sector	Acquirer	Share of voting rights
2000	Shoei	Real estate & electronic components	M&A Consulting (Japan)	2%
2003	Yushiro Chemical Industry	Oil & coal	Steel Partners (US)	9.0%
	Sotoh	Textiles	Steel Partners (US)	12.2%
2005	Japan Engineering Consultants	Services	Yumeshin Holdings (Japan)	over 20%
2006	Origin Toshu	Retail	Don Quijote (Japan)	30.9%
	Myojo Foods	Foods	Steel Partners (US)	23.0%
	Sun Telephone	Information and Communications	Dalton Investments (US)	14%
	Hokuetsu Paper Mills	Paper & pulp	Oji Paper (Japan)	3.4%
2007	Tenryu Saw Manufacturing	Metal products	Steel Partners (US)	8.1%
	Sapporo Holdings	Foods	Steel Partners (US)	19.3%
	Bull-Dog Sauce	Foods	Steel Partners (US)	10.0%
	TOC	Real estate	DaVinci Advisors (Japan)	about 10%
	ATL Systems	Information and Communications	Japan Asia Holdings (Japan)	18.9%
	Solid Group Holdings (formerly Livedoor Auto)	Retail	Ken Enterprise (Japan)	0%

Note: Vote participation rates are at the time when the tender offer is launched

Source: Nomura Institute of Capital Markets Research, based on various news reports

Over the past few years, the management teams at many listed companies have spent considerable time and effort on the question of what type of takeover defense would be best, and many of those companies that have decided to adopt such defenses have worked hard to gain approval at their general shareholders' meetings. This has resulted in a rapid increase in the number of listed companies adopting takeover defenses since 2005, and currently over 600 companies have done so¹⁹. An overwhelming percentage of these have adopted a poison pill approach²⁰, which is based on providing advanced warning. The revival of cross shareholding is evident in the data on the cross shareholding rate, which bottomed at 11.1% in 2005 and resumed a rising trend, to 12.0% in 2006 and to 12.3% in 2007 (Figure 5 above). There is concern that this trend represents a backlash and rolling back of the open approach to decision-making that has been gaining ground at general shareholders' meetings recently.

V. Conclusion

In Japan, general shareholders' meetings fulfill three functions. The first is to make important business decisions, as provided for under the *Company Act*. The second is to monitor the performance of internal directors, i.e., management appointed by the board of directors. There are two types of governance models in Japan, but because

¹⁹ Based on a survey by Nomura Securities. Starting in 2008, however, there have been some companies, albeit a minority, that have voted against adopting takeover defenses, including Shiseido, Nihon Optical, and Nissen Holdings. We attribute this to changes in tender offer rules and to the negative opinion that investors have of takeover defenses, and we think more companies may opt against such takeover defense in the future.

²⁰ If a major investor acquires a given percentage (20% , for example) of voting rights, the board of directors can require that investor to explain its intentions. If an independent committee deems that buyer to be an "abusive acquirer", the company can issue stock warrants or implement other defensive measures.

most listed companies in Japan have a board of auditors, which monitor the business decisions made by the board of directors as well as the representative directors' performance of their duties, and because outside directors do not yet play a very active role, the board of directors does not have much of a monitoring function. This makes it that much more important to enhance governance by shareholders. The AGM's third function is to provide advice to management. Although the shareholders entrust management of the company to the management team, they can provide policy advice in both the managerial and financial arenas. AGMs could provide a forum for debate between management and shareholders as to the best way to raise enterprise value. To ensure the three functions noted above work properly, management needs to make the AGM the centerpiece of its investor relations activity, while providing greater disclosure to shareholders, both at and apart from the AGM.

Looking back at the role played by AGMs over the past decade, we can identify areas that have improved as well as future challenges. One area of improvement is the increased level of two-way communications between management and shareholders that has resulted from companies' efforts to make AGMs more open. Second, the improved decision-making function of the AGM resulting from greater proxy participation has made management (internal directors) more disciplined in their efforts to raise enterprise value. One example of this is the recent increase in the number of companies that have given shareholders the dividend increases and share buybacks they have been asking for.

There are also challenges, the first of which is to improve the content and quality of communication. The 2007 White Paper on Shareholders' Meetings showed that despite a large increase in the total number of statements made at AGMs, the number of statements addressing specific proposals is actually in a slight declining trend. Many of the statements appear to be complaints over products and services made by individual shareholders, who comprise the majority of meeting attendees, speaking as consumers. Individual shareholders should be making statements and asking questions at the meeting from the shareholders' perspective, which we think would lead to a constructive dialogue with management. A second challenge relates to the problem of the company securing votes behind the scenes. There have apparently been cases recently where the companies have either secured votes on their own proposals, primarily from institutional investors, or proposed compromises to shareholders about to make a proposal in order to get them to withdraw that proposal. The problem with this is that when a company puts too much effort on getting shareholders to vote for its proposal, the dialogue between management and shareholders may wind up moving away from management's long-term vision and become short-sighted. A third challenge is communication with nonresident investors. Although efforts have been made to make them more open, AGMs held by Japanese companies probably still feel closed to nonresident investors. Statements from nonresident investors, who are pure investors, may at times be painful for management to listen to, but their harsh words are likely to provide clues as to how best to increase enterprise value. We expect AGMs held in Japan will be able to overcome these challenges and play an even more important role in the future.

	1997	1998	1999	2000	2001	2002
AGM trend						
Macroeconomic & regulatory environment	<ul style="list-style-type: none"> *Sanyo Securities and Hokkaido Takushoku Bank fail, Yamaichi Securities voluntarily shuts down *Easing of rules on acquiring treasury stock (Special Procedure Law on Cancellation of Shares) *Introduction of stock options *Simplification of merger procedures *New laws, and stronger penalties, for extortion 	<ul style="list-style-type: none"> *Government injects jpy1.8 trillion into 21 major banks *Early Financial Correction Law (to conduct ex ante regulatory rulings on banks) is passed *Easing of rules on acquiring treasury stock (capital reserves temporarily allowed as fund's source) 	<ul style="list-style-type: none"> *Government injects jpy7.5 trillion into 15 major banks *Mothers, a new stock market for startups, is established *Rules established on share exchanges and transfers 	<ul style="list-style-type: none"> *Share prices in Japan and the US reach their peak during the IT bubble (Jan-Mar) *Rules on corporate splits established *NASDAQ Japan (now Hercules), a new stock market for startups, is established 	<ul style="list-style-type: none"> *US-based Enron fails after discovery of accounting fraud *Restrictions on treasury shares lifted *New rules on minimum stock trading lots established *Rules on stock warrants introduced *Increase in variety of share types *Introduction of online voting at AGMs 	<ul style="list-style-type: none"> *US-based Worldcom fails after discovery of accounting fraud *US-based Arthur Andersen shuts down *Introduction of preferred shares with rights to appoint and dismiss directors *Introduction of rules on companies with committee system
Major AGM-related events	<ul style="list-style-type: none"> *Incidents of sokaiya demanding protection money uncovered at more than 10 well-known companies 	<ul style="list-style-type: none"> *Court decides lawsuit demanding overturning of Sumitomo Corporation's AGM resolution 	<ul style="list-style-type: none"> *UK-based Cable & Wireless makes hostile bid for unlisted IDC 	<ul style="list-style-type: none"> *M&A Consulting launches hostile bid for Shoei 	<ul style="list-style-type: none"> *M&A Consulting pursues proxy battle with Tokyo Style 	<ul style="list-style-type: none"> *Shareholder Ombudsman proposes that Sony disclose director compensation, and has repeated that proposal every year since then
Investor trends	<ul style="list-style-type: none"> *PFA starts interviewing asset managers on their exercise of voting rights 	<ul style="list-style-type: none"> *PFA publishes research report on pension fund's corporate governance *Japan Corporate Governance Forum publishes Corporate Governance Principles *Former Mitsui Trust & Banking has first vote abstention (effectively a "no" vote) *US-based CalPERS announces corporate governance principles for Japanese firms 	<ul style="list-style-type: none"> *PFA revises investment guidelines, requires its asset managers to act in the PFA's interests 	<ul style="list-style-type: none"> *PFA publishes Fiduciary Responsibilities Handbook 	<ul style="list-style-type: none"> *PFA publishes practical guidelines on exercising shareholder voting rights *GPIF starts asking asset managers to advise of their proxy voting record *ISS Japan established *IRRC agrees on joint venture with Mizuho Securities to provide proxy advisory services 	<ul style="list-style-type: none"> *PFA starts internally managing stock investments *Japan Securities Investment Advisors Association publishes guidelines for proxy voting in discretionary investment *Research Institute for Polices on Pension and Aging establishes voting rights guidelines for pensions funds

2003	2004	2005	2006	2007	2008
Boom in hostile acquisitions					
Introduction of takeover defenses					
Revival of cross shareholding					
Greater exercise of shareholder voting rights					
Shareholder proposals from activist funds					
Rejection of company proposals					
<p>*Industrial Revitalization Corporation of Japan established</p> <p>*Nikkei average drops below jpy8,000</p> <p>*Japan Independent Directors Network established</p>	<p>*METI establishes Corporate Value Study Group to propose ways to deal with hostile takeover bids in Japan</p>	<p>*METI together with the Ministry of Justice, publishes takeover defense guidelines, and proposes plans that are both legitimate and practical when introduced under ordinary conditions</p>	<p>*The Company Act is enacted, making it possible to pay quarterly dividends and to give the board of directors the authority to distribute surplus funds</p> <p>*Online disclosures based on changes to articles of incorporation made possible</p> <p>*Tokyo Stock Exchange publishes report on preparing rules on listings when takeover defenses are introduced</p>	<p>*Subprime loan problem emerges</p> <p>*Company Act goes fully into effect, removing restrictions on triangular mergers</p> <p>*Companies are required to disclose reasons for holding AGM on same day as other companies</p> <p>*Removal of restrictions on where AGMs can be held</p>	<p>*METI's Corporate Value Study Group publishes report that primarily concerns takeover defenses and raising director accountability</p>
<p>*Steel Partners launches hostile bids for Yushiro Chemical Industry and Sotoh</p>	<p>*BellSystem24 issues large number of new shares to Nikko Principal Investments Japan. Former major shareholder CSK's injunction is overturned</p> <p>*Mitsubishi Tokyo Financial Group acquires preferred shares in UFJ Bank, opposing the Sumitomo Mitsui Financial Group</p>	<p>*Livedoor acquires shares in Nippon Broadcasting and launches battle over management control</p> <p>*Murakami Fund's bid to acquire over 20% stake in Osaka Stock Exchange not approved by the FSA</p> <p>*Murakami Fund acquires shares in Hanshin Electric Railway, which later merged with Hankyu Holdings in 2006</p> <p>*Yumeshin Holdings announces stock split and change in purchasing terms in its hostile bid for Japan Engineering Consultants</p> <p>*Rakuten acquires TBS shares and proposes business merger</p> <p>*Proposals to change articles of incorporation are overturned at Fanuc, Tokyo Electron, and Yokogawa Electric</p>	<p>*Don Quijote launches hostile bid for Origin Tosho</p> <p>*Oji Paper launches hostile bid for Hokuetsu Paper Mills, Hokuetsu allots shares to Mitsubishi</p> <p>*Steel Partners launches hostile bid for Myojo Foods</p> <p>*Growing number of cases where changes to articles of incorporation that are likely to be opposed are split off from other proposals</p>	<p>*Steel Partners launches hostile bids for Tenryu Saw Manufacturing and Sapporo Holdings</p> <p>*Tokyo High Court labels Steel Partners an abusive acquirer in its hostile bid for Bull-Dog Sauce</p> <p>*Tokyo Kohetsu's resolution to merge with Osaka Steel is rejected at AGM</p>	<p>*MoF and METI Ministers advise against TCF's direct investment in J-Power</p> <p>*Opposition of Steel Partners and other shareholders results in rejection of Aderans' reappointment of seven directors, including president</p>
<p>*PFA establishes Standards for Exercising Shareholder Voting Rights, and provides external asset managers with a system for automating decisions</p> <p>*Pension Fund Association for Local Government Officials asks all of its asset managers to exercise voting rights</p> <p>*Council of Public Institutional Investors publishes an opinion paper on corporate governance, listing the fiduciary responsibilities of public pensions</p>	<p>*PFA publishes standards for determining the independence of outside directors when exercising shareholder voting rights</p> <p>*IRRC establishes office in Tokyo (acquired by ISS in 2005)</p> <p>*GovernanceMetrics International establishes office in Japan</p>	<p>*PFA publishes standards for shareholder voting on takeover defense proposals</p> <p>*ABP, the Dutch government pension fund, turns over all governance issues for Japanese stocks to UK-based Hermes</p>	<p>*ICJ launches electronic proxy voting platform for institutional investors</p> <p>*Japan Proxy Governance is established</p> <p>*Glass Lewis establishes offices in Japan</p>	<p>*ISS advises voting against 80-90% of takeover defense proposals</p> <p>*Ireland's public pension fund, the UK-based BBC's pension fund, and Denmark's occupational pension fund PKA all turn over the handling of corporate governance on Japanese stocks to Hermes</p>	<p>*PFA opposes nearly 40% of takeover defense proposals (versus less than 10% until 2007)</p> <p>*The Asian Corporate Governance Association (comprised of US and European fund managers and pension funds), proposes to Japanese companies more efficient use of capital, an increase in outside directors, the abandonment of poison pill plans, greater transparency at AGMs, and a reduction in cross shareholdings</p> <p>*ISS and Glass Lewis call for opposition to nearly all takeover defense proposals</p>