



The Asia Foundation

Conference Notes

The Future of Corporate Pensions in the United States and Japan

Sponsored by: The Asia Foundation (TAF), The German Institute for Japanese Studies
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In co-operation with: Nikko Financial Intelligence, Inc

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Place: Hitotsubashi Memorial Hall, National Center of Sciences

Thank you very much for waiting ladies and gentlemen, we would now like to begin the first Global Forum 2003 co-hosted by Asia Foundation and Keizai Doyukai.

On behalf of the organizers, I would first like to call upon Miss Aiko Okawara, Chairperson of the Global Forum of Keizai Doyukai. Miss Okawara, please come to the podium.

Good afternoon and welcome to the first Global Forum event of the year, which we are proud to present jointly with The Asia Foundation.

Our forum will be divided into two parts. In the first part we will have two keynote speakers followed by a 5-minute break to rearrange the room, and then a panel discussion.

Recent scandals in major corporations around the world have rocked the stock markets and shaken investor confidence. Flagrant accounting misstatements and omissions by companies such as Enron and World.com in the US, as well as several scandals involving Japanese companies have highlighted the need to come to grips with the issue of corporate governance. We are indeed fortunate today to have so many distinguished and eminent experts on this subject.

I would first like to call upon our first speaker, Doctor William Crist, who the past president of the Board of Helpers, which is the world largest institutional investor. Doctor Crist is also the Chairman of the Board of Pacific Pension Institute and a Member of the Executive Committee of the Council of Institutional Investors and its former Co-Chair.

He is also a founding member of the International Governance Network.

Please help me to welcome Doctor William Crist.

Crist:

Thank you very much for the invitation to share my experience and views with you. I have visited in Tokyo as a spokesperson for Pension Fund investors of the United States for more than 10 years.

First time I came I was invited to speak on the matter of corporate governance and as I mentioned to a friend of mine just before the meeting, the press, the Tokyo Press at the time referred to my coming as “The return of Black Ships”. I can assure you that it was not my intention to appear to be Admiral Perry, nor is it now. In fact, in these conditions, at this time, across the world we have a common interest in making sure that our businesses, our corporations can exchange ideas, technologies, and capital in a way that is unfettered or unrestrained by lack of understanding, by lack of transparency, by lack of certainty, by lack of confidence.

We have had, as the Chairperson noted, recent examples that have been most outrageous and

outstanding in their size, in their magnitude, and in their effect on individuals and on institutional investors; such instances in the United States, the most infamous are the Enron and the WorldCom, many others, but just to mention the two most commonly spoken names. There is nothing at all that happened in either of those cases that had not been predicted about some corporations, that it would happen. But in both of those cases, the Corporate Board appeared on paper, appeared as it was described, as we read our resume, to be pretty good. That is to say that had independent directors among them, indeed the majority they had persons of reputation, persons of experience, they in both cases had shortcoming of too close a relationship, in my opinion, in our opinion between the Executive Management of the companies and the Directors, but they had independent audit activities, and independent nominating activities.

The fact of matter is that neither of these companies was really very transparent. And the reason why they didn't give an honest face to the world was that there was a combination of intentional deceit, a combination of what could be described as fraudulent activity, and on the other hand, the unwillingness, or inability, I think more unwillingness, of the Directors of the Board that has fiduciary responsibility to the shareholders, to the owners of the company, to do what they were supposed to do, to pay attention, to be critical, to tell the management, and question the management that, you know, this doesn't feel right. There is in the post-Enron, post-World.com world good deal evidence that there were those who indeed did not feel right, that knew that there was difficulty there, but they didn't do the work that it took to uncover this and to bring it to the market's attention.

One of the things that we feel most strongly about, at CalPERS and other large institution investors in the United States, is that Corporate Boards should be more critical of themselves, they should be more self-evaluative, that is that should evaluate themselves in view of their responsibility to the owners of business and to the other stakeholders for that matter.

They should not just be rubber-stamps, or they should not just be persons who sat in a place called the Board meeting, and rely entirely on the information given to them by the Executive Management and then follow that lead. They should be critical; they should be always the inspector, always the investigator.

One of the problems with American boards is that there is too much of building the Board in the image of the previous board, or building the board in the image of the Chief Executive Officer.

The tendency is for the Chief Executive Officers to have too much power, too much control, which can be abused unintentionally by selecting their friends, literally their colleagues from other business to sit on their board, and then they are sat on the other person's board.

And there are examples of directors in the United States that sat on as many as eight or ten

Corporate Boards.

I submit to you, I argue, that no human being can do the kind of job that is necessary, to be the guardian, the supervisor, the overseer, the watchdog, the investigator, the critique, all of those things of, in a modern, complex modern corporation, whether is a Japanese corporation, British corporation, or French or American corporation, because it takes more time to just read and understand the material and to actually do the job, than you have if you are on eight or five or nine or ten different boards.

So what happens, what is happening in a lot of boards around the world is that there really isn't any conscious effort to do what the Board is supposed to do, or too little. I've said just in a few conferences I've spoken at in the last few days is that I've sat and visited many Corporate Boards where the biggest question that they had to deal with was what times is lunch, or more likely, what is for lunch, and what time is the tea time at the golf course, can we get finished here in time to go out and play eighteen holes.

I'm not joking, these are actual statements by people who have responsibility over, in some cases, billions of assets, and tens of thousands of job, tens of thousands of employees, and the pension funds of these tens of thousands of employees going into their old age. And they don't take it seriously enough.

In the United States the executives in most large corporations are paid way too much money. Executive compensation is a major problem in the United States. It is not so much a problem in most other parts of the world, in that there is more of a market balance, but it is a little bit of a problem everywhere. But in the United States there is a tendency for compensation committees to have the attitude that if our Executive Director is to be better than the other company's Executive Director, that person must be paid more. And you have what, I'm an economist by education and by early practice, and indeed a labor economist and we study wage trends and tendencies and we all know in this room that wages of all kinds have a tendency to wretch it up, but they rarely wretch it down. They wretch it up to failure, and they collapse to zero quite often, but they don't wretch it down.

So this is a problem that has to be addressed.

Another problem that has to be addressed and it is a global problem, because really all of these things I mention to you in the short time we have.

I would say, by the way, here that we have many differences, corporate legal difference, corporate cultural differences, traditional differences; things are not the same in Japan as they are in the United States in terms of the way we practice our business over a long period of time. And in this business of corporate governance in which all sorts of organization all around the world are publishing these principles and guidelines, as I mentioned, they look very much alike, but we all understand that there is not one perfect size that fits every culture, and every

system the same. But there are practices that are better and practices that are worse.

Now back to what I was saying that we see is another major problem. And that is the international problem of accounting, of being accountable, and of the practice of accounting. One of the world's great accounting firms ____ is no more. If you were a college student and you are studying accounting and you talk about the big number, whatever the number is, the number has diminished, and continues to do so.

Accounting is very important to businesses, and those who audit those accounts are very important to those business. Honesty, and accuracy, and reliability, are an indispensable part of a free market. Because without those *free* markets, where prices are determined in a public world are going to be biased by something other than reality. The only test of the value of the exchange of anything, I think most of us in this room would agree, is what it takes to clear the market. And if you don't know any of the fact, really, because they are misrepresented either intentionally or unintentionally, then what can you do.

When I used to teach my classes in economics I would upon the board the Marshallian cross, and I'd say: "You've go supply and map demand and there is the price. That is the price and that the quantity that we exchanged and I know that quite precisely." I can say that because this was an abstract example. And what did that Marshallian cross, that supply-and-demand curve presume? It presumed perfect knowledge; it presumed knowledge on both sides of the market, what the conditions of the market were.

But if all of those actual conditions are kept from our eyes, our eyes - the institutional investors or individual investors, then we're acting blindly and not in the best interest of anyone

In the United States following the terrible examples of Enron and WorldCom, the US Congress went about the business of passing a law. Quite often that is not a good thing in United States and in Japan; but, nevertheless, the politicians did this and did this very quickly. And the President of the United States signed that law in a very, very fast fashion, because it was politically acceptable to do so. The law was called Sarbanes Oxley Act and set about to correct some things in our market place and had an impact on markets around the world that I and others (not that I am so smart or that intelligent), we had been saying for fifteen years needed to be dealt with, that needed to be corrected.

There is not a lot there in the way of saving us from inaccuracy and from cheating and from fraud and from just bad behavior by Boards that don't pay attention, but there is a new focus, a more of an emphasis on paying attention to these things that there had been before that law.

And one of the best elements of that law is a creation of something called the Public Accounting Oversight Board. This Board, which is a very small group of five people, has tremendous authority and power to do investigating work, to go into modern corporations' activities and to see how their accounting is done, and to evaluate it, and to take action, to act

as a policeman as well as an investigator. One of my best personal friends in the world, a person who was my general counselor and helper for many years has had the honor of being appointed to that Board. And the best thing about this Board is not that she is on it (although she is plenty tough and smart to do what needs to be done); it is that it has the support, the financial support and the backing of the political strength of the US government, at least at this time.

The other good thing about all of that awareness in the US Congress was that the Securities Exchange Commission which had existed for a long time and didn't have its role particularly changed, but it was provided greater honor, greater credit, by being given more funding, more money to run itself, so that it could hire more staff, better staff, and do what it's always said should be done, to cause the exchange of securities to work more as it should work in a free price system.

So these are general things that have happened in the United States, and I knew you would be interested in. I'll turn the rest of my time to a couple of comments just about corporate governance itself.

The term is kind of misused sometimes. Sometimes people write: "we need corporate governance". Well, ever since we had the first joint-stock company in the 17th century we have had, whenever there was any kind of ownership in parcels, there had to be some kind of governance or regulations.

The modern corporation in Japan and in the United States and elsewhere has a system, which can work with or can work without good governance, but they all have governance. So we don't just want corporate governance, we want *better* corporate governance. And that effort is difficult, cause all of us, while we would ever say we don't want better corporate governance, would anybody in this room say you don't want better corporate governance? I don't think so. But what has to happen to achieve that sometimes is very difficult.

The size of a Corporate Board, for example, needs to be a workable thing. If you have a corporate Board with 20 or 25 or 30 people, that's not a good corporate board, I'm sorry. It's just very difficult. But in some places it is very difficult to lower that number, because of how it got to be that size in the first place. A Corporate Board that has no outsiders, or no independent directors is not as good as one that does.

In some places like Japan, I understand very well that obtaining diversity on the Board by getting outsider independent directors is very difficult because of the relationship of corporations throughout the modern history of industrial Japan.

It is less difficult in the United States and even there though we have a tendency not to do that. We have a tendency to get people from other places and bring them on our Board and call them independent, but if you look closely, they play golf every Sunday morning with the same

Chief Executive Officer or they are real chums with each other somewhere else, or indeed they come from the same industry, and they come from the same part of town so to speak, so that they're essentially clones of each other. That's not a good Corporate Board situation.

Why, why is CalPERS, and other organizations like that in the United States and other parts of the world, so concerned about these things? Well, we're pretty sure, or I'm pretty sure that they are responsible for the retirement money of 1.3 million people. There's lots of Boards of Trustees around the country with these responsibilities. And yet even though I'm fond of reading a very old quotation of some scholars who wrote about security analysis way back in the 1930s. Ramon Dodd wrote, and some of you are familiar with this quote, it was written in a book in 1934: "The choice of a common stock is a single act. Its ownership is a continuing process. Certainly there is just as much as reason to exercise care and judgment in being a shareholder as in becoming one."

Well, I believe that to be true. I believe in that to be especially true for shareholders like big pension funds, because the owners of the shares are the members or the beneficiaries. The holders go to proxies and exercise judgment on their behalf. It is very important that we advocate for the best interest of those shareholders, and it is not inconsistent with advocating for the best interest of the economy, for the best interest of the environment, for the best interest of human rights, for the best interest of equality of treatment. This notion that somehow you can't direct your cooperation in a way that focuses on the shareowner interest without harming other stakeholders, I submit to you as a false conclusion. In fact, quite often it is, if you will, an excuse for not paying attention to business in such a way that will look to the shareholder value as a number one consideration of the operation of the company.

There is a lot of evidence now, for what it's worth, that institutional investors especially are willing to pay a premium when they buy the equities, when they buy the common stock of companies that have been judged to be governed well, that is that have good corporate governance. A study by the McKinsey organization, it is about a year-and-half ago now, was fairly impressive, and showed the premiums of substantial amount will be paid. I believe that going into the future the ability of companies, of incorporated companies around the world to attract the least expensive capital funds they can, will depend increasingly on how their business is governed. And all these variables that I talked about and these lists of rules and best practices, like independent audit committees, independent nominations committees, the Chair of the Board and the Chief Executive Officer being different people so on and so forth, all of these, well will come to bad.

I'm just about out of time and I don't have time to go through all of the different US principles, the core principles and so on that most of the groups in the United States stand for, but that

doesn't trouble me very much, because they can be read in a thousand different places now. Even the OECD publishes principles and guidelines, and every organization has these listed. And making lists of these things is kind of easy. The International Corporate Governance Network, of which I am proud having been one of the original organizers, and some people in this room I know have attended conferences of the International Corporate Governance Network, a very valuable organization today, because it allows people to talk together, it has its own list of international or global best practices, corporate governance principles. They are so good that even CalPERS simply adopted them as their own and put them in their guidelines, but they're just words, just words on a sheet of paper, good words, but just words on a sheet of paper.

What does it take, and this is my conclusion, what does it take to improve corporate governance in Japan, and in the United States, and in the United Kingdom, and in France? What will it take in any of these places? It takes investors with leverage, investors with particular voice, investors with influence because of the size, to assume the responsibility of causing it to happen. And that's why I'm proud of the work that CalPERS has done over the last dozen years, because we have voice, we have made noise, we publish lists of companies that we believe are not governed well, we give awards to the companies that we believe are, we go and meet with companies' boards and point out: "you can improve, we want you to improve because we're not going to sell your stuff, we don't sell your stuff, we buy and we hold, we're long-term holders of equities, we represent a source of patient capital, which is important to the world."

But we've not done a good enough job. It is our responsibility to enforce these principles, to cause these guidelines to stick, to convince you as business leaders that it's in your best interest and in your shareholders' best interest, and therefore not against the owners of other stakeholders, but in everybody's best interest, if we pay attention to how our corporation are governed, we seek diversity, we seek honesty, we seek transparency, we seek good audited books that everybody can look at, and we seek, considering all these things in our best interest in the long-run.

Thank you very much.

Okawara: Thank you very much Dr. Crist. Our next speaker, Mr. Bill Emmott, is the Editor-in-Chief of the Economist, and the author of the book "The Sun Also Sets". His latest book is "20:21 Vision: Twentieth-Century Lessons for the Twenty-first Century," and we look forward to the Japanese edition, which will be published in July. Mr. Emmott tells me that he also accepts credit cards. Please help me welcome Mr. Emmott.

Emmott:

Thank you very, very much, Okawara-san, for the kind introduction and for acting as my marketing manager, and thank you all for doing me the honor of having me this afternoon and helping me to return to Japan where I lived from 1983 until 1986, and which I continue to think of as my second home. My job this afternoon is to give a personal perspective as a financial journalist, or economic journalist, as well as the professional perspective of an editor of a weekly magazine, which happens to be sold in every country in the world, and therefore very, very international professional perspective.

What I'm sure you all realize, is that journalists, including economic journalists, including international journalists, are quite awkward people. We don't really behave very well. We have beards. We don't comb our hair. We are outsiders. We often ask awkward questions. We write articles that people don't like, if they are the subject of the articles.

My argument to you this afternoon, in this context of corporate governance and disclosure, is quite a simple one, and that is that I want to try to persuade you to take the view that although we are awkward, although we are outsiders, we are actually extremely useful outsiders. We are useful to companies because we are outsiders and, therefore, because we have an independent view both about the outside world and about the company we're writing about. But we are also, and this is important, most useful to companies when we are, in fact, highly independent outsiders. A vital point about being a journalist, particularly I think a financial journalist, is that it is very important to be independent, it is very important not to become too close to the people and the organizations that you write about, whether they are governments, or companies, or just celebrities. It is very important, if you like, not to have any friends among the people that you write about. Personally, I find it very easy not to have friends, but it is very important to be very separate from the subject you're writing about, and I would suggest that the second part of my simple message to you, is that journalists, the media, are also more useful to you as corporations if they are not your friends, if they are independent of you. They are better outside rather than being brought inside.

So this is my simple message. Let me elaborate upon it a little bit.

My elaboration of my view of the role of journalists in corporate governance and disclosure begins with a simple point, and that is that the duty of the media, the duty of journalists, is to provide our readers or viewers with information, with analysis, and with, frankly, entertainment. We hope to make our readers think, but also hope to make them enjoy the process of thinking as well as hope that they understand the world better.

Secondly, of course, as I have already implied, this role of being a duty to the readers produces a psychological reality about journalists as outsiders producing on behalf of readers and not companies or governments. Journalists are, or should be, naturally suspicious or skeptical

people.

At a conference in South Korea that I attended this weekend, a German businessman, in one of the panels, described the media as, and I quote, “people who seem to wish to make life difficult for politicians and executives”. He meant this as a criticism, I consider it to be praiseworthy. Although, of course, with my type of magazine, it’s worth pointing out that while we try to make life difficult for politicians and executives, also many of our readers, perhaps even most of our readers, are executives and politicians themselves.

The third point that is worth saying though is that when we write about companies and about business in general, we have a lot of different purposes in our mind. The controversy over scandals that Dr. Crist talked about, Enron or WorldCom, or in other countries, Credit Lyonnais in France, or Snow Brand in this country, or Mitsubishi Motors, these controversies, and the current concern about corporate governance might imply that journalists are only interested really in writing about dishonesty and wrong-doing. It might imply that we see ourselves as a kind of investigator, or detective, but that isn’t true. It is one of our interests, but it is only one of our interests, and it is not actually our most important interest. Our most important purposes, as financial journalists, are that we want on behalf of our readers to explain *what* companies are doing, to tell stories about their successes and their failures, to compare their performance with that of other similar companies, and, above all I think, to find lessons for managers and investors. We want to understand the business and the company; we want to know about the people and the organization. We want to find out about the quality of its products, the type of ideas that the company has and the type of management that is in place. And of course, we want to have a sense of how well, or badly, the company is doing. You may well think, when I’ve given this great long list of things we want to know about, that we want to know too much, that the journalists are people who get in the way of process of business, rather than someone who is useful. I want to convince you that that’s not the case, that actually we are a helpful pressure point on companies.

But first let me explain a little about this process. Just as corporate governance is not a new phenomenon, and just as there is no single set of principles about corporate governance, really there is no panacea, there is no simple solution, so the important thing to understand as a journalist about companies is that they are very, very varied in their type. They are different when they are private companies from when they are public companies. They are different if they are run by entrepreneurs from when they are run by managers. They are different when they are big from when they are small. And they are different when they are domestically oriented companies from when they are very international companies. In my experience, this is true within countries just as it is between countries, and that actually the variety of types of companies is the same all over the world. When I was stationed in Japan writing financial

journalism, I found just as much variety in the approach and nature of Japanese companies as I did in Britain or in the United States. One should not, I think, look at countries with national stereotypes in mind.

What does this make it seem to journalists that is important in disclosure of information, and the approach of companies to journalists. Well, we would say a few things. First thing to know about journalists is that we are, of course, very busy. Editors, and I'm sure my stuff agree with this, editors are demanding and often unreasonable people. This means that journalists operate in a hurry. One consequence of that is that journalists, though they are suspicious people, they actually tend to want to trust what they are told. They'd rather start by assuming that information they are given is accurate. The importance of that observation is that once journalists find that the information they are given is not accurate, or that they have been told things that are not true, then their trust is completely broken, and they tend then to run to a completely opposite judgment.

As a journalist operating in countries around the world, I have often found that I have been given false information. The result of this is that the organization or company that has given me this information is immediately, and probably for a very long time, an object of great suspicion. It's hard to re-build the reputation once you've lost it.

Secondly, we want consistent information, we want information to be in the sort of form that we are able to analyze, to explain how things have changed; we want information to be comfortable. Countries do vary in this, in my experience. In the United States, there is, of course, a lot of disclosure of information. SCC filings, quarterly reports, analysts' reports based on information given to them by companies, reports and studies done by the companies themselves, often one feels as a journalist that you are swimming in information. What we now know, or what we have been reminded about by Enron and WorldCom cases, is that the quantity of information is a different matter from its quality; that even if there is a lot of information it can be dishonestly provided.

Companies do vary a great deal. Enron did provide quite a lot of information and was, in many ways, quite open to visits by journalists and interviews by journalists. Some other companies, like Proctor&Gamble for example, are rather closed; they don't like visits from journalists, they try to keep journalists away. Other companies, in my experience, disclose full information, and then don't like it when you write about that information. We recently wrote an article about Goldman Sachs in The Economist, about the disclosure of a new compensation plan for their executives, based entirely and perfectly accurately on their filing to the SCC, and they were very angry with us for doing this, it was almost as if they were outraged that somebody should have actually read the information they had disclosed. So things do operate in confusing ways.

In Britain, too, I would say there is less disclosure, quite a lot less disclosure; there's more secretive behavior, use of nominee companies, but generally a culture of accessibility to journalists.

Some things become obvious as you go over time as a journalist. The media is part of the problem, that's one of the things that's obvious. We like personalities, we like Chief Executives that are prominent, but actually the prominence of the Chief Executive is often an indicator that something may be going wrong with the company, perhaps because they are too focused on the celebrity and too little on the company. We as media often help to create interest about the awards, prizes, given to the Chief Executives, to marketing directors and finance directors, in fact, experience suggests that ranking in the Businessman of the Year awards in different countries are often a very good clue as to which of the companies are soon going to fall into trouble. I also find that sort of complaints that one receives after an article has been published are quite revealing; they are often as revealing as the interviews that take place. I shall never forget a complaint that I received when I lived in Japan from what was then the Japan Tobacco and Salt Public Corporation. I've written a short article about their competition with foreign cigarette companies and they called me back into the company and they have taken my article, and they cut it up into separate sentences from the magazine, pasted these sentences on a big piece of paper, and took me through the article every sentence, trying to argue as to why I was wrong. This actually convinced me that I was right and, therefore, I felt they told me more about the company than I could have found out any other way.

I'm currently in a legal case in France with the Credit Lyonnais bank; their Chairman has sued me for libel. I shan't comment on the case cause the verdict hasn't come through yet, but one thing that's interesting about the case is that the question in the article (which is about a scandal at Credit Lyonnais to do with an American insurance company that the company bought), the question, really, the issue is whether the Chairman of the company knew about this scandal, or as we said, whether he should have known it. And one thing that's revealing about the way the company was run in those days is his defense as a witness in the court case a few weeks ago. His defense was essentially one of incompetence; his argument, quite honestly and straightforwardly put, was that actually he did not know about the scandal because he was too disorganized to know about this scandal. As I say, what the verdict in the court case turns out to be I cannot speculate upon, but this also told me a lot about the company.

What are my conclusions? Generally, of course, we write about corporate governance and in writing about corporate governance, we feel that accountability and independent scrutiny are the important things as Dr. Crist said. We feel that there is no simple system there, there's no guaranteed rule. We feel, though, that in terms of disclosure of information, it is better to be full and open about information, but also consistent with information. I say that although there

is really a choice for companies, I think, a choice for companies either to be very, very open, to give out a lot of information, to be very accessible to interview, or I think to be very closed, and not provide a lot of information. My experience and observation is that both of these two choices are quite practicable and possible choices, but the middle path is not a very good choice. Giving a little information, just giving *some* information, providing *some* access, is not usually a good choice. It is better to be very open, or to completely keep the press out.

But finally, and I repeat really my simple point in this short amount time available. And this is that, my view is that journalists are, of course, difficult people, we are nuisances to companies. But we are also, I believe, part of the process of independent scrutiny, of checks and balances that is part of the process of corporate governance. We are useful to outside investors, because we are doing the same job as they are doing trying to understand the company, but we are also, I think, useful to inside the company, to managers in the company, because we are an indicator of what customers may think, how they may react, we are an indicator, certainly, of what investors may think, we are an indicator of what public opinion, in general, may think, we are an indicator of how a company compares to competitors, we are an indicator of how company looks on a global basis.

We are certainly not perfect in providing this information, this check and balance, we are amateurs, we are often not expert at all, but we are people whose actions can be used and learnt from if the company is willing to provide information, to disclose information and to be open. I found as an editor during the process of coming up towards the war in Iraq, that the letters and emails I was receiving from the readers were very useful. I was taking a very strong position arguing FOR the war in Iraq, and most of the letters I received were critical, they told me that I was wrong, that I was mad, that perhaps I was on the pay of George W. Bush. Serious letters, of which there were many, were very helpful to me in formulating my own arguments, in helping me understand my readers, in helping me understand my own market. I believe that good managements, good companies can and should try to use journalists as independent critiques, as independent examiners of the company, and then be able to learn from our reactions, learn from our analyses, learn from our inquiries. You cannot do so if you seek to control journalists, but you can, and you must also, be tolerant of journalists. But if you are those things, I think I may say humbly we can be useful, even if we are often awkward and difficult people.

Thank you very much.

Okawara: Thank you very much, as I mentioned before, we will have a five-minute break and reorganize for our panel discussion. See you in five minutes.

So if we may, I would like to get started on our panel discussion. We have a great panel today gathered in this one room, any one of our panelists could probably give a two-hour keynote address on the subject of corporate governance, so we are indeed honored that they have agreed to share their opinions with us. Dr. Crist and Mr. Emmott have already been introduced, the other panel members are Mr. Junichi Ujiie, Chairman of Nomura Holdings and who, I hear, holds a PhD from the University of Chicago. Unfortunately, Mr. Ujiie has had some important business, which he was not able to foresee, and will have to leave after the preliminary remarks of the three panelists. Next is Mr. Shotaro Watanabe, Vice-Chairman and the Executive Director of the Keizai Doyukai and former Vice-President of Kao Corporation; and Mr. Gary Evans, chief strategist of HSBC Securities Japan.

I would like to start out by asking Mr. Ujiie, Mr. Watanabe and Mr. Evans, to spend about five minutes in response to the two speakers, in drawing upon their experience as independent directors, or in describing how their companies address the issue of corporate governance, or perhaps in discussing the difference between Anglo-Saxon style of corporate governance as opposed to the Japanese style of corporate governance. We are especially interested in hearing about how Japanese companies are reacting to the new Commercial Law, enacted on April 1, which allows companies to make a choice between the new type of committee-based governance, and the old-style of governance by having statutory auditors on the board. So Mr. Ujiie, thank you.

Ujiie (translated)

Thank you very much for the kind introduction. I am Ujiie.

In Japan, as was mentioned, the revised Commercial Code has gone into effect, as of the 1st April, and therefore, the companies have the choice whether to maintain the traditional system under the Boards of Statutory Auditors, or to shift it to a committee-based new system. For this fiscal year, most of Japanese companies are expected to continue to maintain the traditional Statutory-Audit-Board systems. For this fiscal year, the public companies that would shift to the committee-based companies are expected to be around thirty, including Sony, Toshiba, Hitachi, Mitsubishi Electric, Conica, Hoya, and so forth. By the way, our company Nomura is one of the thirty or so that has decided to shift to the committee-based system. Now, the framework of this committee-based system, I think there are two key essences.

Number one, traditionally under the Board-of-Statutory-Auditors systems, the role of the Board of Directors was divided for the roles of the Directors and the Executive Officers, and the new role of the Board of Directors is to supervise other management and the basis of operation is now going to be delegated to Executive Officers. As for the decision-making of the management, there would be a larger scale of delegation from the Board of Directors to the

Executive Officers. As a result, there is an expectation that more flexible management led by the Executive Officers would be a possibility.

The second essence of the shift to a committee-based company, as we have been hearing repeatedly, that there will be more transparency in management. We also wish to strengthen the supervision over the management.

Three committees, including the Audit Committee, Compensation Committee, and Nomination Committee will have to be established; this is an obligation. With regard to these three committees, the majority of the members must be external directors. With the establishment of this system, the traditional Statutory Audit Board System will be abolished. In the case of our company Nomura, in the end of June, we have the annual general shareholders' meeting. With the approval at the general shareholders' meeting, we plan to shift to this new system based on committees.

But the reason why we decided to shift to the new system is because in the past, the Board of Directors had to wear two hats, but in comparison to that, if we clarify the roles between the Directors and the Executive Officers, we thought it would be easy to follow and understand. Another reason, under the system of committee-based framework, this would be in line with the corporate reform that we have been already following over the past years. What we mean, as of October 2001, we decided to shift to Holding Company System, we established new organization called Nomura Holdings, at the time, we had slightly more than ten directors; we decided that two of these members should be external directors. Now, in the past, Nomura Securities was a public company, and the number of directors was somewhere between thirty and forty. And when Nomura Holdings went public, the number of directors was slightly curbed, and two of those directors were external directors. So, the external directors were included among the members.

We established a Compensation Committee, and what we call Order Committee, which is the Executive Management organization.

So this was already the background and, therefore, shifting to the new committee-based system was easy for us to follow, as it was only an extension of the reforms that we had already started. We want to avoid misunderstandings here, but the point is, that we are NOT going to shift to the new system because we think there is a deficiency in the traditional audit-based system from the corporate governance perspective; that is not the case. We do not want to lose any advantage of the traditional audit-based system, but under the new framework, we believe that we need to continue thorough review as to what care we should take to manage the company.

Right beside me, we have Mr. Watanabe; he was with KAO in the past. KAO is a company known for the most advanced activities in corporate governance. With the revised

Commercial Code, KAO has decided *not* to shift to the new committee-based system; they have decided that they would maintain the traditional Statutory Audit Board system, and they shall continue to strengthen corporate governance, that is what I have learnt.

On the other hand, Nomura Holdings, and the major company group is Nomura Securities, we do not have splendid, brilliant track record like KAO; however, still at the shareholders' meeting in June, we plan to shift to the committee-based system. What I am trying to say, whether it is Nomura or KAO, we share the common goal of good corporate governance. So we are in the same country at the same era, however, our approaches are not the same; we are following two different approaches. This is my message here.

Now for corporate governance purposes, I don't think there is one single correct answer as to the most desirable structure. In order to ensure adequacy of our corporate governance, serious discussion has to be continued. But I don't think we will reach one single correct structure for all organizations. The legal system, essential structure, the era, or the climate for each and every company's issues will be different, which means that the optimum corporate governance system should also be different companies.

In the debate on corporate governance, rather than trying to extract one single correct answer, I think it would be helpful for all of us if we tried to accept the diversity and try to learn good practices from others.

And from this kind of perspective, I would like to raise two examples, comparing the American and Japanese approaches. And the first point is about the requirement of external directors. In order to effectively supervise management we do need outsiders' perspective, and I think this is common to Japan and the USA. However, what exactly does 'external' or 'outside' or 'independent' mean? There is a major difference in the criteria in the USA and in Japan, when the word 'independence' is certain in the USA, that one should not have been a director of that particular company in the immediate past of three years, and this 'immediate past' of three years is going to be extended to the 'immediate past' of five years, and the requirement that they should not be receiving anything other than compensation of the directors from that particular company.

On the other hand, when we talk about external directors in Japan, the criteria are more rigorous. If the person has worked for that particular company even for one day, at any time in the past, they do not qualify as external. If they have worked at least for one day for the company in the past long time ago, they are considered to be subjugated to the company; I do not understand it. These are too rigorous criteria.

The point here is whether Director can maintain the independence at all times. So this person, I believe, needs another source of income other than the company where they are going to hold the directorship. Even if that person might not work for a different company, if they are going

to depend solely on the income of that company, it might be difficult for the person to be purely independent.

But having said that it is not easy to write the legal language, I understand that we do need to depend, at least to some extent, on formal criteria. But honestly speaking, I really do not understand why we have these Japanese criteria. But this particular area, I think, the working criteria is closer to what we find feasible.

Now the second observation is my feeling about American situation. In order to ensure the adequacy of supervision, I compare the USA and Japan. First, in the USA, there are sections 302 and 404 in Sarbanes Oxley Act; I am not going to deal in detail with the legal discussions, but in order to comply with 302 and 404, all the business operation flows related to financial report would have to be printed on paper. The company has to certify that there has been no error in any part of the business operation flow, according to my understanding, which means a huge amount of paperwork would be required, which means we spend a lot of cost; however, despite increasing cost, I do not know whether the adequacy of supervision will be enhanced. My understanding about the USA is that they always pursue efficiency and are a rational country. That is my respect to the USA, but even in this USA that I respect when they face a big problem like Enron, all of a sudden, the Pentagon restrains violently back.

On the other hand, in Japan in addition to the external directors, normally you would have a non-external director as a member of the Board of Statutory Auditors, who knows very well about the company. So this director who is not external would review the company regularly on an on-site basis. That is how we are trying to ensure adequacy. Rather than spending too much time and expenses and paperwork, utilizing someone who is familiar with the company situation amongst the auditory members, we think is more efficient and effective.

So whether it would be the external requirement for Japan, whether it would be the requirement according to Sarbanes Oxley, I feel that the rule simply is forcing us to comply with formalities. As we have heard in the keynote speeches, rather than formalities it is more important for us to think about the contents, about the substance that would generally allow us to conduct supervision in an effective and efficient manner.

In our company, we do have auditors that have long experience in the company plus a mix of external directors, so the non-external auditors are always in the company, they attend important corporate meetings, they frequently ask for reports from people related to company, which means that they are always supervising on-site.

I am sorry I spent a little more time than 5 minutes, but the newly-allowed committee-based is more close to the American system, rather than the traditional system. Just because we have become closer to the USA, we do not want to see a situation where our corporate governance has deteriorated. In the USA, where the board is mainly made up of external directors, there

must be some kind of careful attention given so that the supervision of the management does not end in a superficial ritual.

I wanted to learn a great deal this afternoon, however, as Ms. Okawara had told you, unfortunately, because of other business, I have to leave now, sorry, thank you very much for your kind attention.

Okawara: Next, could I call upon Mr. Evans to brief us on your comments.

Evans:

Thank you. Perhaps I should explain, first of all, why I am here, or who I represent apart from myself. Like Mr. Emmott, I was formerly a financial journalist as well, and an editor of a financial magazine although a much less prestigious one than the Economist, I should say, so I have some empathy with his comments on the level of disclosure. What I do at the moment is that I am the Chief Strategist for HSBC Securities, and in that position I spend a lot of my time talking to institutional investors. From that perspective what I see is that the level of interest in corporate governance from foreign investors, European or US investors, is extremely high, and has been indeed for many years. The level of interest still amongst Japanese institutional investors, I am afraid I find is still rather low. As the Chair Person said, I could probably speak for two hours about corporate governance, it is such a broad area. But there are two things that I want to do in the time that has been allotted to me.

First of all, is to sum up how I saw the two keynote speakers, who were both extremely interesting from different points of view. And secondly, to try and suggest some areas that we might go into in the panel discussion.

So in the summary, first of all, in very simplistic terms, it seems to me that Dr. Crist's main message was that in the end it was up to investors, I think he said that the investors needed to use their leverage and their influence to assume the responsibility for improving corporate governance. I will come back to that in a second, but I really do think that is the key for Japan, it is not something that just the companies must do, this is something that the investors must take the initiative on doing. And Mr. Emmott's speech was very much about information, and disclosure, and scrutiny. And that clearly is a key as well, but I have to say it is an area, in which seems to me there is a risk that Japan could go backwards, maybe this is something we can talk about later. But the government's natural reaction here, every time there is a fall on the stock market is to say how can we change the accounting regulations to hide some of the problems. We hear at the moment that the LDP is trying to allow companies the option not to market their securities holdings, to hide the problems. Frankly, from the point of view of an investor, we can work it out anyway, it does not really matter. But that natural reaction to try to

hide things is, I think, a big shame.

Secondly, what I would like to do is to suggest some subjects, the two big areas that I think we might go into. The first is to think about corporate governance from a macro point of view. And it seems to me, and has seemed for some time, that actually corporate governance is the one key problem with the whole Japanese economy, and it is the one problem that the government does not talk about. But why it is a problem is if you analyze why Japan has gone through twelve years of essentially a recession, with very little growth in twelve years, it comes down to poor returns on capital. Why are the returns of capital poor? They are poor because the managements of a vast majority of companies, and of course there are some good exceptions, including many people here, but the vast majority of company managements are not focused on maximizing profits. Why are they not? Because the corporate governance system is set-up to incentivize management to worry about their employees, to worry about market share, etc, so improving corporate governance could well be the key way of improving the performance of Japanese economy.

That brings me on to the second area that we might talk about which is practical suggestions how you should do that. How do you get companies to improve corporate governance, or get investment institutions to put more pressure on companies? I think at the corporate level, the changes in the Commercial Code potentially will help, but as Dr. Ujiie said, only maybe 30 companies this year are taking it up. And it worries me that the problems in the USA in the last year give a rather good excuse to Japanese companies, to say that actually US corporate governance is not so good, maybe we should just rely on the old-style Japanese corporate governance. But for example, there are other laws you could introduce. Unfortunately, the law that had been proposed to make it compulsory for every company to have an external director was in the end dropped, when the Commercial Code was changed. And what I should tell you, and this is not reported widely in Japan, is now every major country in Asia, including China, has a law insisting on at least one outside director, in some cases, half of the board have to be outside directors. Japan is the one exception.

And the second side of that from institutional-investor point of view, how do you get institutions to start to put more pressure onto companies to improve corporate governance. Well, there are a number of ways how you can do that, but perhaps the most effective, which I would be very interested to hear Dr. Crist's comments on, would be to introduce something like the ERISA Law into Japan. The ERISA Law in the US puts an obligation of diligence on institutional fund managers to take an active role in the management of companies. And this was something that MITI, as it then was, was hoping to introduce to Japan, and it was dropped. But there are some quite practical changes like that that I think could be made.

Maybe these are some things that we can talk about later. So I think I had my five minutes, let

me finish at that point.

Okawara: Thank you very much. Next, I'd like to call on Mr. Watanabe for his comments. And perhaps you can also touch on the white paper on corporate governance issued by the Keizai Doyukai.

Watanabe (translated)

We have just heard from Dr. Crist about the example of CalPERS and the frustration he's feeling towards the Japanese market, and the complaints vis-à-vis Japanese companies, and from Mr. Emmott we have heard that from the perspective of a journalist, with regard to information disclosure there were many pieces of advice, and I'll touch upon what Mr. Emmott said later on.

Since my time is quite limited, my first comment is, as has been referred to, at Keizai Doyukai. Last year we came up with a recommendation for over white paper for corporate governance, and that is enhancing the corporate competitiveness. And this is the white paper which has been issued by Keizai Doyukai, so based on this, I would like to provide some comments vis-à-vis what Dr. Crist has said. This white paper by Keizai Doyukai reflected results of a survey we conducted roughly a year ago. As a matter of awareness of the management, we asked what they thought of the current size of the Board of Directors. A number of twenty or thirty directors was mentioned, and most of the Japanese managers feel that this is too large. 70% of the respondents are saying that the Board of Directors and Executive Officers should be separated from each other. As far as introduction of outside directors concerned, 60% of respondents said that outside directorship should be introduced. But who would be the good candidates for independent directors, how do you assure that they are truly independent. I am now an outside director of ISETA, a department store, and Dr. Crist mentioned various characteristics of typical independent director, and in case of Japan, he said the CEOs are 'chums'. So whether we can truly be honest with each other, I do not know if it is true or not, but in the case of ISETA department store, I received a card of ISETA, but, of course, I never benefited from a discount, not even one yen, on any purchase I have made in this department store of ISETA.

And concerning the number of outside directors, I do not the time to go into this in detail, but maybe later on I will have a chance to comment on this.

And the third point has to do with establishing committees. Dr. Ujiie mentioned that based on the Amendment of the Commercial Law, with a US-style corporate governance, thirty Japanese companies have adapted committee-based corporate governance. Last year I went to Beijing University and I met Chinese counterparts, and Hong Kong and Taiwanese

academicians and scholars, Mr. Inoue of Toyota, he was an auditor, and I have spoken about a new style of corporate governance, we had a symposium with Chinese academics, and at that location I said that there are four different types of companies. As represented by thirty companies that want to adopt the US-style corporate governance, that is one group.

The second group, KAO, or as Dr. Ujiie has mentioned as well, that we might adopt the US-style, but we might be more cautious about adopting the US corporate governance style. In the case of KAO, we have two outside directors at the moment, we have established a committee, but that is not according to the format, which is called by the amended Commercial Code, and therefore, we want to accustom ourselves to the committee-type format. I think maybe a large share of Japanese companies belong to this second group. I cannot give instruction to what KAO corporation will do, so I cannot define the choice which will be made by KAO, but with the elapse of time, perhaps we will move on to a different category. So the second group of Japanese companies watch over what is going on with the thirty companies that belong to the first group, and as Keizai Doyukai survey shows the result that, when asked whether by the amended Commercial Code the Board of Statutory Auditors will be reorganized, there were only about 9% of the respondents who said that they will transform the organization. But if the thirty companies of the first group do succeed, I think more Japanese companies will shift to the first group.

The third group are large companies belonging to Keizairen, typical examples being Toyota or Canon, that are very proud of the results and achievements that they have come up with using the Japanese-style corporate governance, and have no intention to change, but how they will be evaluated by the market is something we have to watch out for.

The fourth group of Japanese companies are those that lack efforts in terms of corporate governance, and they are not dealing with corporate governance as in case of Toyota or KAO, and maybe a large number of Japanese companies belong to this last, fourth group, and that is one of the causes for the stagnation in Japanese stockmarket.

So the thirty companies are pioneers trying to succeed, and if they are positively evaluated by the market, that will determine the future prospects of Japanese companies. And if the first group is positively evaluated, because the Japanese companies are rather flexible in nature, I do feel that more and more will shift to the first group.

With the passing of the time, I would like to conclude, and maybe add more comments later on to the discussion.

Okawara: You heard Mr. Watanabe explain that although his company, along with Sony and Toshiba, have decided to adopt a new form of governance using independent directors and committee-systems, the majority of companies, like KAO, have decided at this point to

continue with the old system, however, introducing certain particular forms of governance. And Japanese corporations in general are undertaking to change their corporate governance guidelines. What do you feel is the most important aspect or point that may be explored for change, Dr. Crist?

Watanabe (translated)

May I just take one more minute to add another point? I forgot to mention this last point I had to say. Besides the committee-based governance system, Keizai Doyukai pointed to the selection process. We felt that that was the first and foremost issue, the selection process. So if we try to maintain the current Board of Statutory Auditors, that will not do, and therefore we need independent directors to participate as members of committees to be set-up. And that is one of the very big recommendations made by Keizai Doyukai. I forgot to mention that point, so allow me to mention that point.

Crist:

First, just to observe, as we all know that change is always slow and sometimes it seems that the first step how to get to the long mile, it does not seem to be taking place, but it is taking place, with the new Commercial Law and many other things that Mr. Watanabe just mentioned. Just the last one, I think, is very important, recognition that the selection process or the nomination process of members of the Board is critical, if you're to have independent (whatever that means, we have not an actual technical definition of that but if we had), to have a truly independent Audit Committee, or Compensation Committee, or the other important committees that were mentioned. That process is one that in the United States and in continental Europe is not strong enough, but we have not worked hard enough on that. We are working on that now through forcing, as much as we can through the voting of proxies, new nomination procedures and causing nomination committees to be independent.

I wanted to go into the way the question was asked in terms of something that Mr. Evans said is an interesting technical point about the law in the United States that covers what we call the Taft-Hartley Plan or the Employer-Sponsored Labor Management Plan, is the ERISA Law. What the ERISA Law requires is participation in the form of voting proxies. All shares owned must be voted if they are owned by pension plans that are under ERISA. Government, or public, pension plans in the United States do not fall under the ERISA Law, but in every instance, it is the policy in CalPERS, for example, to vote all proxies in all places where it is possible.

That is one way, it is the first way, that this responsibility to try to move towards better corporate governance, of course, must take place. And I would mention one specific behavior

of large American pension funds, and also in the United Kingdom, now as an example. When CalPERS determines on how to vote on any particular proxy issue in any company, as soon as that determination is made, it is placed on our website, so that anyone with access to the Internet can go there and see, how we intend to vote on any issue for any company, for directors, for compensation, for anything. And the explanation of why, we are learning that that sharing of communication is a way to get wider participation, to do, as Mr. Evans pointed out, get leverage to make more responsibility for getting management to focus on improving profits. I think that could work everywhere in the world. Of course, voting proxies is very difficult in some places including Japan, for different reasons, it is not as difficult as it was ten years ago, but the fact that annual general meeting are all held at the same time, the same day; it makes engagement very difficult, and is thwarting much of this emphasis.

Just one other comment, with specific reference to something that Mr. Ujiie said. The specificity of some of the requirements of Sarbanes Oxley, he mentioned very specifically sections 302 and 404, requiring reporting and signing-off, what we refer to as the veracity of the reporting. I agree that it is too much paper, and of course, you can just pass it on, and pass it down, and you end up not necessarily with much more accountability. But in the United States, at least, that is a start, because it does cause people to commit to paper and to put their name on something, which upon scrutiny by journalists or analysts or others, can then put the light on something, when in fact that has been the case.

And, of course, a very important remark, that supervision of the management should not be a ritual. That really is what good corporate governance is all about. And in many places in the world, it is kind of a ritual. So everything we are advocating for, I think, is to move away from that.

Okawara:

Thank you very much.

Going further with Mr. Evans comment building on Dr. Crists' statement, Mr. Watanabe, why do you think that the ERISA Laws were not enacted here, or similar laws. And how do you think we can get institutional investors in Japan to be more of a lobbying group for governance, as CalPERS is throughout the rest of the world?

Watanabe:

About the ERISA, I cannot go into too many details, but currently in Japan we are trying to reform the pension system. We are looking at the future of the social security, and there are numerous problems. Also in the public pension system, we are facing the situation of aging population, low interest rate, low returns. All that environment plus the pension system itself is

having a problem, which is that smaller number of the younger generation has to support the growing aging population, and we are at a certain deadlock.

At the same time, the pension societies in the companies, the retirement benefit system within the companies was successful, because they were established at a high-economic-growth time in the past. Now our longevity has become even longer, we now enjoy living longer and longer, therefore even the private pension system is also facing problems; in fact, some of them are really facing bankruptcy. So Japan's social security problem is unlike the ERISA in the USA, and I believe that it is going to be difficult at this time to try to reinforce our system.

At Keizai Doyukai, we have made recommendations about pension reform in the past year, about the corporate pension societies and also about the private pension systems. We are going to review and offer further recommendations, about the background, the defined contribution (are we expand the DEC portion, or are we going to stick to the DEP-defined benefit system, how our we going to combine these?), thinking about all that, we will continue to discuss even reflecting the situation of the ERISA in the USA, as we further try to reform pension system.

About corporate governance, in 1993 I went to the USA and Europe, about nine years ago, I had to visit investors for IR purposes. I am making annual visits to the Western societies, which means that the majority of institutional investors are now familiar with me. I personally have had significant contact with the investors, almost like CEO, I directly spoke with the investors. Through this personal process, if we conduct appropriate IR, transparency and accountability, in fact, makes companies grow. That is what I have learnt, we become cultivated about IR to be transparent is very difficult for us human beings; when you are transparent, people are staring at you, it is not easy. But you have to stand strong, at the same time, you have to become more competitive, that is the difficult environment, and that difficult environment makes the companies grow. That is what I have become convinced of.

As far as transparency and accountability concerned, it is not that the Japanese dislike this concept; not all Japanese are vulnerable or weak, but looking at the social context of the past, without rigid rules Japanese companies were able to survive so far, so we certainly do like certain aspects of transparency and accountability, at least, at this stage. Now, we were talking about WorldCom and Enron scandals in the USA, and after those scandals we have seen revisions in the systems, we were talking about corporate governance post-Enron, post-WorldCom, so the Japanese people are saying: "Well, you see, not everything American is good, look at WorldCom and Enron, look at American system, what is good with the American system?" There are some Japanese people who are thinking in this manner, however, as I mentioned about recommendations issued by Keizai Doyukai, after all, we cannot stick to the pure Japanese corporate governance system, because when we visit IR in the Western countries, they tell us to become more comprehensible to the outsiders, they ask

us to be reliable and trustworthy in a constant way, that is the message we hear from investors. That is why many, an increasing number of Japanese CEOs, are traveling overseas for IR, and they are becoming aware of the requests and needs of the investors, so I believe there is going to be a major advance in this corporate reform some time in the near future in Japan. I am rather optimistic.

Okawara: What do you think of Mr. Watanabe's remarks, Mr. Evans?

Emmott:

Maybe I can just make some further remarks about the investment institutions. As Dr. Crist said, change tends to start in very small ways, and I think that there clearly are some signs of improvement. One of the most encouraging signs I've seen recently was the new rules that have been drafted by the Pension Funds Association, the Rengokai, which has some what-seem-really drastic rules on how it will vote its proxies. If I am interpreting them right, it is saying that basically any company that has made, I think it is, three years of executive losses, that it will vote virtually against every resolution at the annual meeting, that sort of thing. I would be slightly skeptical about whether in practice people do that. But at least now, in public sector, some of the institutions are starting to think like this.

I think the problem is probably even deeper than that, and there are maybe two problems. One is the cultural problem, that it is very hard for Japanese fund managers to go along and vote against a large famous company. And if you look at the record of voting on proxies, or voting negatively by Japanese institutions, what you find is that they vote three times more negative votes for foreign companies they have shares in than for the Japanese companies they have shares in.

The other problem is I think one that exists in other countries, in which it is always very hard for private sector institutional investors to vote against companies. It is much easier for institutions like CalPERS, which does not run any corporate pension money of its own, than it is for a major asset management company, which manages companies' pensions, to go along to another company and vote against a resolution on the board. So that is a problem that exists globally, I don't think there is much you can do about that. It just means that public institutions have to take the lead, and they are all starting to do that.

The second cause is that is more specifically Japanese, which has to do with the structure of cross-holdings. It is extremely difficult for, let's say, a large insurance company, to vote against the resolution of pretty much any company that it has shares in, simply because it does business with lots of other companies. That sort of cross-holding structure, I think, does make it much harder for corporate governance to work. Cross-holdings clearly are now reducing,

but from the point of corporate governance, the quicker they reduce, frankly, the better.

Okawara: Would you like to rebut that?

Evans:

I will just make a quick comment, with reference to the pension funds and the difficulties of having good, sound pension funds in all countries now, and in Japan with the pension fund reform. You have mentioned the Japanese Pension Fund Association, which I think is doing some very important and valuable work in Japan, and in the last two days I have been meeting with representatives of this group. And at the present time, I am the Chairman of the Board of the group, which is introduced as the Pacific Pension Institute, which is encouraging of learning across the Pacific of the pension funds that are in Japan, and in the USA, in Thailand, and so on, but also are becoming more aware of the relationship between both private and public investment in equities by these pension funds and the importance of it, and how you really have to have a good clear understanding of what you are doing to make all of that work. The kind of success of a pension funds is so very important across the world because of the demographic trends, which in Japan are more apparent than in most places, but which exist everywhere. The link between that activity and good corporate governance is very, very real. An important comment on something Mr. Watanabe said, investor relations (IR), 20 years ago when I first started doing this was amounted to showing some slick papers with some nice pictures of what the business is supposed to do to someone who did not understand, and there was no intention to cause him to understand. With good IR now as Mr. Watanabe has done, I even practiced it with his company, so it seems good, is a different thing, and now it really does have to do with informing shareholders around the world in a very real sense. The first time I visited companies in Europe and the IR person would bring out to me the quarterly reports and the annual reports, I said "I do not want to see these, these are not useful to me, I want to see your audit books, I want to know what this company is planning to do for the next ten years, not what pretty pictures you took in the last three months". And so I believe worldwide that has changed, much for the better, and is part of what, I think, we agree is necessary to have a better capitalism.

Okawara: Excellently put, any comments on that?

Emmott:

Yes, I would just like to, I must say I also agree with the last comment, but also just to reinforce a point that Gary Evans made earlier about the role in this issue of incentives. The question I

was trying to ask myself is what is the incentive to change? What is the incentive to operate in a different way? And I think, as we have been hearing about the realities of the circumstances of many Japanese companies, because of the nature of their investors, and often because of the type of organizations and the way they work, is that there is not much incentive to change. And I think one can, I am sure, focus on whether or not these incentives can be changed, and what might change them.

Incentives tend to be set both internally in an organization and externally. Internally, in an organization, the incentives are set by the senior management, especially by the Chief Executive or the owner, to some degree by colleagues, by peer pressure. Those tend to work in a different way when the company is clearly run by an entrepreneur, Mr. Honda, or Akiyo Morita, and his colleague in Sony, or Mr. Matsuhita, than later on when the ownership and management change.

But there are also set externally, the incentives, by the degree of competition, by the desires of owners, by the requirements of the government, by the changes and requirements of public opinion, by the changing requirements of the customers. We have seen in the United States, I think in the last ten or fifteen years, the power of incentives in changing behavior, as there was more competition, more demands by investors, more deregulation, more opportunity given to executives to make a lot of money through the stock options, the shares, and that had a very, very powerful effect on the way companies behaved, and also on the growth in productivity and in profits. We also saw, though, how incentives can lead you wrong as well, in the incentive that stock options gave to executives often to lead their companies to a bad course, and to enrich themselves. As Alan Greenspan was asked a few months ago, whether he thought it had been a greedy period during “the bubble” in America, and he said that the amount of greed in human beings was unchanged. What had changed was the opportunity for greed, and the incentives provided to human beings. And I think that is a very important issue behind corporate governance debate.

Okawara: Mr. Watanabe, as Mr. Emmott mentioned, the Anglo-American corporations rely on incentives, such as stock options, to help align the objectives of the management and shareholders, which have their good points and their bad points. However, in Japan’s socially egalitarian society, executive pay is aligning with a pay of other company employees and consequently, Japanese executives are not very well compensated as their Western counterparts. Good, not good? Can we have your comments.

Watanabe:

In the case of the United States, as we mentioned, perhaps the level of executives’

compensation is too high, and in case of Japan, it is too low, and it is too low around an average level of compensation. So I am not recommending that the Japanese Directors' compensation should be raised to the level of the United States, however, if the compensation is to be performance-based, based on the rules Japanese companies should extend appropriate compensation to the directors. And that is one major agenda, which has to be recognized by Japanese companies. And that will also elucidate who will be the most appropriate candidate for directing that company. And markets should be able to support this. Whether we will be able to succeed in constructing a relevant system, we should realize this proposal.

I have talked about incentives, and for formation of a stock price, a company may be enthusiastic about improving corporate governance, perhaps it will earn a three-year premium on its stock price, and if there is such an index, perhaps everybody will be really zealous about it. However, the stock prices seem to fluctuate, we have increased earnings and increased revenue for many consecutive years, and for the stakeholders sustainability is the source of happiness. Growth has to be sustainable, prosperity has to be sustainable, and that is most valuable for all stakeholders. And when I went to an IR trip to Boston, I received a question that when KAO will continue to increase revenue, to increase earnings even by one yen, consecutively year-by-year, and if it will continue, KAO will never go bankrupt. But I was criticized that is not corporate management, ROE and ROC, I am talking about the sustainability of ROE and ROC, but it seems that the investors in Boston are more shortsighted in terms of the stock price in the market.

And perhaps that is one source of confusion for corporate management, to tend to have such mild views about the stock price.

There was a mention of the topic of IR, of course, the time unit is one-hour, and when I make these IR speeches, in the beginning I ask whether perhaps I should jump right into the question, or perhaps make a prelude to the fifteen-minute presentation before entertaining questions, and I ask my audience, my investors, every time which is their preference, because I tell my colleagues in the companies that analysts and investors outside the company are more knowledgeable about KAO, that is the reality, that I have discovered through the IR activities. It is not that you are not interested in beautiful photographs and beautiful annual reports, quarterly reports, and even Japanese companies realize that IR is not about these beautiful photographs.

May I continue on? Mr. Evans, many pieces of advice, many demands by Japanese companies as well as institutional investors or else the Pension Fund Associations, maybe the PFA is quite laggard in taking action, they were quite late in realizing this, and from corporate management perspective, I think this is only automatic that they have to opt for that, the PFA. And it so seems that the PFA has a free hand, that companies like fisheries or other general companies,

they have to look into the insurance agreements of the employees and they also have to look at the stock-market connections, and therefore the supply-chain may be rather complex in case of such companies, therefore in the Japanese society there is very complicated human network and connections, and of course, this is being dissolved at the moment and shareholding is being unwinded, and supply-chain is also being reformed because this will not serve to maintain competitiveness, so everything that has been taken as relative is now being winded up. However, there is tendency for Japanese to want to procrastinate and even the deposit insurance was postponed as well. But the more we postpone into the future, the timing will be less opportune, and it will worsen. By postponing the shift to full deposit insurance lifting, I think Japanese sector will suffer from even more difficulties. LDP legislators, some of them are talking about freezing market value accounting, but in one of the meetings we had with Keizai Doyukai, we have decided on the rules, and because the closing of the account for the last year has finished, we should not be retroactive in looking back into the closing of the account, which has already taken place in the end of March, and this way we will risk losing credibility in the market. And it is a conclusion drawn by Keizai Doyukai that we should not do that.

Evans:

I would like to make a comment to a point that was made earlier, that mentioned that there is a tendency perhaps for many Japanese to look at the examples, we have mentioned Enron and WorldCom, there are many others in the United States and in other countries, but to say, perhaps you know, that the form of corporate governance that they advocate is not so good. I would suggest that that is a very bad way to go and a bad way to think in that the efforts that have been made over the last fifteen years have caused many, many American corporations, and corporations in other parts of the world, to change to the point where they have become reliable, their information has become dependable, their auditing has become really good, and their reporting is good. And they have become more efficient and more effective producers, because of that. The hundreds of corporations, and pension funds particularly, such as CalPERS talk with every year in an ongoing dialogue about how they can improve their governance and thereby become more effective, and this has perhaps saved untold numbers of additional companies from going down the path that hunted these companies. So it is not that the system fails, it is that we have not pursued the system with enough diligence.

And as to the incentives to change, and as to the timing when Japanese Pension Fund Association may do something, I think, that the general economic conditions of the world right now are such that everyone in every country is getting more focused, and more concentrated on the notion that we have to do everything we can to cause the free-market

system to work because it is all we have left. And we're becoming a very dependent of society worldwide in the advanced industrial nations, very dependent on small number of young people to produce a lot of surplus to take care of a very big number of old people. And that is a big problem, so if the corporate structures are not themselves changing in a regressive way to take advantage of diversity and of independent thinking (again, however, whatever that means), but good attentive board directors, we just cannot do things the old way anymore, because the world has become too complex and too negative. We have to be more aggressive, that's why, I mentioned before the specific Pension Institute, the whole idea of this organization is to share intellectually across the Pacific Ocean to better understand our timing and why we do things now, and how to incentivize each other to change. Instead of just making speeches like I am doing now, but to really go to the places of business, and talk about profit in an honest way, and not rest on past practices.

Okawara: Anyone wish to...?

Evans:

Maybe I will just throw in a couple of subjects here. We are getting broader, we are getting very broad, but in broader subjects, if you think back of history of corporate governance in Japan, and as Dr. Crist said there is no such thing as saying "we want corporate governance", there has always been corporate governance, but how is it operated in Japan? Well, essentially by the banks. The problem, therefore, comes down, I think, a lot to the whole system of banking in Japan, that banks are no longer able or willing to operate the system of corporate governance. So to a large extent what we have got know is either a vacuum, or at least we are in a middle of a process from going from banking-center corporate governance system to having a market-driven corporate system. We are still rather in the middle, which leaves a vacuum. The problem with the vacuum is that it allows a lot companies essentially to do whatever they like. Their governance is internal governance, the people there are running the companies on behalf of those companies. So number one is banking.

The second problem is linked to that, which is who are companies run for. And I think if you gave that question to any company in the USA, or indeed in the UK, without any exception they would say: "Well, it is run for the shareholders". And they mean it. In Japan, if you ask companies that, a few believe they run it for the shareholders, they are quite a lot who know they have to sort of say that if a foreigner asks them, so they will say they are run for the shareholders. But there are still quite a large number of Japanese companies, who, very openly say... I visited (I won't tell which company, but) a very well known large company, together with a corporate governance officer of a major international institution, and he asked this

company: “Who you run for?” And you could see the person at the company thinking do I give them the answer they want or do I give them the real answer, and in the end he was brave and he gave the real answer, which is: “This company is run for the good of society”. And that is such a vague concept, it seems to me, it does not mean anything, so I think that is the problem; from the point of view of an investor, and I think from the point of view of efficient running economy, companies have to be run for the sake of their own, for their shareholders. And one final comment is how do you get the society or any society to believe that. Well, you have, I think, to shift the balance whereby the people realize that they benefit if the companies are run to make profits. And at the moment in Japan, the vast majority of people think that it is better that companies do not fire people, do not try to maximize their profits, because that is going to create extra unemployment, etc. What you have to, I think, get people to understand is that their pensions, in future, will depend on whether companies make sufficient profits to pay them. And there are various ways how you can go about making people understand that, such as for example, having a much larger number of 401K-type defined contribution pensions, where the individuals earning those pensions will realize there is a very direct link between their pension and profitability of companies. So maybe these are thing that can be thrown out for other people to comment on.

Okawara: Perhaps Mr. Watanabe, as the only member of the panel representing a Japanese corporation, you could address the problem of the banks no longer being able to continue governance of Japanese companies, number two, the problem of whether the Japanese companies should move to the governance model, which is basically accountable to shareholders, or should it maintain the model, which it takes into consideration other stakeholders in society. Three, how do you get society to believe that corporations should indeed be run for shareholders. And I think Mr. Evans also mentioned the 401K, which has not always been successful in the US, due to the downturn of the economy, but how should this be approached in Japan, now that the pension funds also are not having very much success.

Watanabe:

First, let me speak of the stock market in Japan. Depending on some of the companies in Japan, they are making their own efforts and therefore performance is improving for some companies. But the evidence is not reflected in higher stock prices because of the Iraqi war and because of the vulnerable financial system, the stock prices do not necessarily rise, plus the fiscal deficit, which is huge. Because of these downward pressures, even if they make efforts, it is not reflected in the stock prices. If you look at the TV broadcasting from the USA, it tells that profit is so and so, that is why the stock market reacted so and so. This is what we hear, which

means that the companies' effort is intimately linked with the stock prices. However, in the case even more than the companies' individual effort, there are stronger forces and the companies' stock prices are drifting. I think this is one unfortunate aspect. So, if you think about companies in major deficit, even if the companies are making efforts, whether it'd be the Downes index or the profit from stock prices, everything goes down. So this is not a normal situation.

Now, for bank-based governance, the companies naturally will have to shift to other approaches. The largest disadvantage of a cross-held situation is, I mean, if the stockholder is stable it might be good in terms of balance of supply and demand, but amongst the top managers, the responsibility, the accountability, will not be pursued rigorously, if there is cross-holding. So we should unwind, as was mentioned earlier, like in the PFA, on a free-hand basis, someone needs to be able to scrutinize the management. And I believe on a gradual basis there will be a shift, there will be a new direction, that is my first observation.

Secondly, a perspective of shareholders, as I mentioned, even if you say shareholders, in Japan most of them are institutional, it is banks, not individuals, or there are insurance companies in Japan, or it would companies that have trading relationships. If I may say so, when you say shareholding in Japan, it is virtually all professionals. Japan is a country where the largest amount of shareholders is all professional shareholders and investors. Now in case of my company, KAO, for 40 years, of course, there were strong forces that wanted to maintain the status quo. So for 40 years it was a battle against the conservatives. Professionals are more conservative, according to my experience, professionals need to maintain status quo, and they don't like change. But we have to change that, and that change can be provided by market forces. But if it is all professionals, and professional cross-holders, amongst companies, because of that situation, Japan continued unchanged. But because of globalization, this cannot be maintained. And even if some try to change, because of macroeconomy and difficult situation, the incentive to change is being slowed down.

I understand that DB will not survive, because a new employee joins the company at the age of 20, and they retire at 65, and can the company be responsible until the company worker dies? So, 60 years they will continue to live after joining the company, and can the company, the management be responsible until that person dies? Impossible, in this changing world.

Now 401K type, that is indispensable, absolutely necessary, but if you expand the 401K system, the social insurance system will become worried about their system going under. The vested interest has to be protected and that is their barrier. But the system cannot maintained, so 401K has to be introduced. If we shift to 401K, what happens is that the general public becomes more interested in stock market, so each and every citizen becomes more interested in stock market, and if there are more people interested, then a healthy corporate governance is

a requirement, because the general public will depend for their life on healthy corporate governance. But it is only recently that individuals are starting to invest, because before the war, no Japanese had savings anyway, after the war we enjoyed high economic growth, and most probably for about 20 years or so, we believed that money should be kept in banks. Or even there is no interest growth expected, we grew up believing that money should be kept either in your cupboard, under your pillow, or in the bank.

Now the time has come, if this is correct, if we shift to 401K system, we have to review about the future. In this financial environment, with this social environment, can we survive and depend on future pensions? Only when the general public becomes interested, can change start. So, the introduction of 401K, I believe, would be the key, as Mr. Evans mentioned, whether Japan changes or not.

Okawara:

I am afraid we are running out of time, so one last comment from each member of our panel. I will hand on the mike to you, Mr. Emmott.

Emmott:

Oh, thank you. Well, my final comment is actually a comment on the story that Gary Evans told about asking someone from a big corporation what was the company run for. The answer, for the good of society, made me think a little bit about two things.

One, though I cannot comment on this actual example, I am sure it was a sincere answer, I wonder if it is a true answer. The truth in many cases is that the companies are run for the benefit of the employees and managers. And society really is not one of their considerations. Their benefit is to themselves, they cover up problems, they do not give information out about cars that do not work properly or products they have difficulties with; they are basically working for themselves. Next question I ask myself is well, if it is for the good of society, has the company actually asked the society, what it thinks? Does the society agree that the company is being run in its benefit? Let's say it was an honest answer, I think, the best way to look at it is to ask how could society tell, how could you measure the answer to the question. And this is what, I think, brings one back to openness of information, so that society can tell in some way whether the company is run for its good.

Secondly, back to the reason why shareholder value is the least bad of all possible answers to this. It is not a good answer because it produces all sorts of analytical problems, share prices go down for bad reasons or good ones, shareholders are greedy people just like anyone else, but it is the least bad answer, one, because it provides a good measurement, at least somebody is making demands from the outside, that are being measured, and secondly, because actually

shareholders have become reasonable proxies, reasonable substitutes for the society as a whole as more and more members of the society become dependent on the integrity of investors from the pension funds, and also insurance companies.

So I think the good of society could be the good answer, could mean shareholder value, but often it is not actually an honest answer.

Okawara: Thank you very much. Dr. Crist, ...

Crist:

Oft-quoted Churchill's statement of democracy is that it is the worst political structure, except for all the rest. I think we might also say that profit-maximizing, and profit-based free enterprise system is really a bad economic system except for all the rest. History is proving that out in how you make that work is by having confidence in the system, of perceiving that it is going to be better, this will make the market rise and so on. And Mr. Watanabe said something very important here about 'confidence', and that working people and all of the citizens, not just the professional investors, not just the big institutional representatives such as myself, but the people have to have confidence in this system. Well, how do they get confidence? I submit to you the way they best get confidence is by having full disclosure, by having a transparent system, that when they see a state of how a company is running, that it admits that it is trying to make profit and so on, that it sees that clearly accurately and honestly, and has confidence, that is the case. We have had too many experiences throughout history the other way, so the people have lost confidence. We have to regain that confidence. And the best thing we can do to do that, I think, is to have improved corporate governance, which seriously will cause us to be more honest and more transparent.

Okawara: Thank you very much. Dr. Evans, ...

Evans:

I would like to comment in a slightly more optimistic note. My comments have sounded slightly negative, it is not that I do not believe that there is no change in companies in Japan, in its corporate governance, I think the situation is clearly moving in the right direction. We have got now thirty companies, as Mr. Ujiie said that taking up this new form of corporate governance. And I think what you will find is that very quickly investors will say: "We require you to have this if we are to invest in your company". And it could well be 800 companies within two years. It is not that the change is not happening, it is just that the change is too slow, and that is something that, I think, applies to a lot of policies in Japan. Some of the items I have

mentioned here, like an ERISA-style law, that would make it compulsory for you to have non-executive directors, all those sorts of things, these proposals have been around, but there has not been the leadership to make them happen. If you contrast that to what happened in the US, when Enron and WorldCom came out, as we heard earlier, the US reacted extremely quickly, they argued too quickly, Arthur Anderson went bust on this, and very, very quickly. And sometimes maybe the US is a little bit too quick, but I think it is better to react to these problems, to shut them down, solve them quickly, and maybe the solution you come up with is only 70% of the best solution, you know, if we had another year-and-half, or five years to write Sarbanes Oxley, it might have been 95% good, now it's only 70% good.

The fundamental problem in Japan is that everyone argues for reforming, for example, banking system for 12 years to get the perfect solution, and in the meantime, there is no solution. So I think changing too quickly (and not perfectly) is better than no change at all. And I think that is probably true in corporate governance as much as anything else.

Okawara: Thank you very much. And lastly, but certainly not least, Mr. Watanabe.

Watanabe (translated):

Clearly, in Japanese economy and Japanese enterprises, we are at a major turning point. We inevitably have to grapple a reform, otherwise there is no future for economy, nor for the enterprises; therefore, corporate reform, after all, has to be dealt with squarely. Recently, Keizai Doyukai also is looking at socially responsible companies, Mr. Kobayashi, our representative, says that this would be the lifework or the final major topic for his position at Doyukai, and we want to issue recommendations, which means companies have to think about all stakeholders. I personally have visited European countries, and SRC, socially-responsible companies, or SRI, socially-responsible investment, is what I have learnt. Mr. Emmott said that should the companies only think about stockowners, shareholders, that is the question we are pursuing. We have to look at the environment, society, we have to think about employment, and at the same time, of course, we have to remember our shareholders. Taking into consideration all that, and on top of that, how can we pursue sustainable prosperity. I think that would allow also the shareholders to win. We have seek approach, and at the same time we have to enhance company's performance. Coming forward corporate managers basically have to think what kind of artistic product they want, that is the artistic product as a company, what image they want. At the same time, you need transparent monitoring system, because if it is not successful, the management would have to be forced to be replaced. That kind of rigorous system is required for corporate governance. So that kind of target should be clarified by the management, we have a group of 1200 corporate executives in our

organization and that effect is made. That is my final comment.

Okawara: I would just like to end the discussion by saying that despite the system and framework of governances that companies can put in place, it does not work unless the board consists of good, capable, honest members with integrity. And this is the most important point as far as I am concerned. Now we have time to entertain a few questions from the floor, so please raise your hand and mention your affiliation.

I am sure the members of the Doyukai have a lot of questions and are not usually this silent. Of course, a lot has been covered.

Q1: My name is Makiko Yamada from Berain Point. The first point that came to my mind in discussing this theme is that Japan has rested on intermediation, indirect finance, so Japan is trying to shift from this indirect finance to direct finance. Perhaps corporate governance, which has been fostered in the context of direct finance, cannot be fostered together with the indirect finance type of governance. Mr. Emmott, when you were living in Japan, why were you able to predict the collapse of 'the bubble' as there was insufficient information in Japan, so that is my question I wish to ask you.

Emmott:

Because 'the bubble' lasted a long time is the only answer. Good sort of principle that one's grandfather tells one is that if something looks to be true, it is always not true. And the evidence accumulated over so many years, and it looked too good to be true and, therefore, it was possible to assume that it was not true.

Q2: I am a Chairman of a public corporation, I am not exactly a management member of a private enterprise, but my question goes to Dr. Crist. According to the earlier heard discussion, as a lesson from Enron and WorldCom, the requirement of external directors or independent directors, the functions of independent directors have been mentioned. Eight or nine companies have been mentioned by Mr. Ujiie, if you are a member of the Board of Directors of eight or nine companies, you might not be able to fulfill the functions of being an independent director. On the other hand, if you become a member of eight or nine Boards of Directors, the question is, where is the income coming from? Fifty-thousand dollars, that might have been the income according to survey, which is about 6 million yen, if that is the income situation, can sufficient time be given to each and every company, can that type of person function sufficiently as an independent director. So they can really be independent

directors? So supervisor functions or auditor functions, I believe they should be sufficient delegations as auditor or independent directors for those persons.

Now in Japan, the statutory members were full-time employees of the company, they were monitoring what the executive officers were doing on a full-time basis, but if they are independent directors, they would only come on a limited time basis. But despite being independent, despite being outsiders, would they be able to function sufficiently? In Japan, if you are shifted to new committee-based systems, then the full-time requirement of statutory auditors would be gone, and we are discussing whether non-full-time auditors can function sufficiently. So that is the question.

So physically, health problems or mental health, if you are an independent director of multiple companies like eight or nine companies, can you function sufficiently, that is the question.

And number two, the economic basis as mentioned by Mr. Ujiie, they can only receive the compensation as an external director from one single company, so unless they have other sources of healthy income, they might not be able to maintain a healthy status as an independent director to each and every company that they sit on the board. So by strengthening the function we might want a stronger system of auditorship and supervision, and there might be some inconsistencies between the established system and the reality. Dr. Crist made his own request, but maybe it would be conducive to what you are looking for, cause I am also an auditor myself, and I am thinking with a sleepless nights.

Crist:

The point is that all good directors, as the Chairman said, first, have to be good people, and honest, and have integrity, and work at what they are doing. To do that, at eight or nine companies at the same time and to do a good job, I submit, is impossible; it is too many, it should be four or five maybe. You need to be independent to the point that you do not rely on the management of the company for your income, for your existence, or you become 'not independent'. There are plenty of people in the world, though, that can be directors in corporations producing any good or service; there has been not enough effort put forward to find these people, or include them in the governance of company. There needs to be, in addition, geographic diversity, I think the time has come when the companies in Japan should have American directors, and companies in France should have Japanese directors, and so on. There should be gender diversity, there should be experience diversity, all that mixed you get a better decision. It is very difficult to find these people granted, it is not impossible, and the risk of liability now is probably better than actually two years ago, so I just think we have to believe that we can find enough people to do this job, and then work to do it.

Okawara: OK, time for one last short questions, Chigusa-san.

Q3: Chigusa from JY. The companies which are represented by the panelists are wonderful companies, and so it seems that corporate governance of Japanese companies is improving in large strides, if we regard the Japanese companies represented here today. However, there are numerous Japanese companies that are being left behind. I have served as an Independent Director of such companies, and one point which came to my notice is that one of the problems experienced in the Japanese boardroom might be really a basic problem, but there is not level of awareness with regard to the realities concerned. I am pointing to the knowledge per se about legal issues, but it is more about posture or attitude, for instance, if there is a question which is not clear, and if there is a suggestion that perhaps a lawyer or a legal counselor should be sought, then it is too exaggerated and I hear oppositions to bringing in some legal counsel. But it is not that we want to avoid an exaggerated situation, that is why I am seeking legal counsel, but since Japanese corporations have to behave with various companies and actors, so unless the realities are cleared, we would not be entertain corporate governance. Of course, there is much room for further improvement in the case of Japanese companies, whether it be the United States, or United Kingdom, or Germany, or other Asian countries, these are the steps that they have gone through to reach the stage that they are in at the moment. So what are the steps that you have experienced in these countries?

Watanabe:

Maybe I can respond from a Japanese company standpoint. When it comes to Japanese corporate governance, we talk a lot about compliance, but compliance should come even before corporate governance. And there is that debate on one hand, and we should not confuse that. And that is one thing that I have become aware of. And if you look at the series of recent scandals, one series is that if there is no compliance, there would be a very severe backlash from the market and perhaps such experience has changed Japanese companies. Transparency over the market, they are the instructors and trainers for Japanese companies, and the corporate governance of Japanese companies must be fostered through such steps. And, of course, for the changes that are called in case of Japanese companies, but responsibility for not achieving enough change seems to rest not in private companies, but more for the government of Japan or the Japanese bureaucracy. That is my understanding of the current situation.

Okawara:

I would like to call upon my partner, in this endeavor, Mr. Andrew Horvat of the Asia Foundation and give us the closing remarks.

Horvat:

Thank you very much. Before I thank all of the co-organizers for making this afternoon possible, I would like to make a comment in Japanese.

(translated) Well, I certainly hope that you had a chance to glance through the documents of the Asia Foundation advancing corporate governance reform in Asia. Frankly, the Chief Economic of the Asia Foundation is responsible for this document, and the Asia Foundation has been very much interested in the corporate governance in the Asian region for many years, which is reflected in this document.

If you turn to page 3, there is a paper entitled “Advancing Corporate Governance Reform in the Philippines”; Mr. Jesus Estanislao is the former finance minister of the Philippines. His first name is *Jesus*, and here we have Dr. *Crist*, so I am sure everything we have heard today is nothing but the truth. Please, forgive me for making such a bad joke.

I thank all of the participants today, and my co-organizer, Aiko Okawara, and also to Bill Emmott, and to Bill Crist, we have made a long journey to come here; Gary Evans, who I once had the honor to work for and with on Euromoney; Mr. Watanabe, who was very supportive of this project from the very beginning; and also I’d like to thank Ms. Yamada here from Berain Point who has also been a great supporter.

I would like to make one final comment, which I suppose is kind of a corogative of some of an organization, who has pushed for this project. I am an ex-journalist and an observer of Japan for several decades, and there was one point which I felt was actually alluded to, but only slightly, which is the sense of belonging, the sense of how do you perceive the truth, the idea of do you have a vested interest in telling it? And I think that one of the aspects of Japan’s corporate structure, which has worked the greatest against telling the truth, is the lifetime employment system. This system is responsible for engendering loyalty into Japan’s workforce, and which has, of course, had many good aspects in motivating workers to work very hard. However, it has also engendered very little responsibility to the society or the shareholders, and I think, as a journalist, I have come across a lot of very honest people, who have worked very hard for the companies, and felt it their duty to lie to me. It was because, I suppose, unlike the United States where if you feel in conflict with the company, what you say is “the worst thing they can do to me is fire me.” But in reality, that means you have an opportunity to get another job. In Japan, with an illiquid labor market, and so much dependence on your connection to your corporation, this freedom has not existed to many people until an economic downturn.

So perhaps there is a silver lining to Japan’s long-term economic recession, and that is, as the

labor market becomes more liquid, perhaps people will be a little bit braver to tell the truth, to blow the whistle, and to talk to Mr. Emmott more frankly.

I shall add that we do have a vested interest in having sponsored this event, and that is that an absence of good corporate governance means an absence of public trust, as I think has been alluded to. But we felt for a long time that perhaps the best cure for Japan's ills is if a certain amount of trust in corporations, a certain amount of trust in corporate leaders, in financial intermediaries, would be restored, and people would return to buying stocks in otherwise good corporations.

Again, thank you very much for making this possible, and I would also like to thank the six participants for their excellent, timely and valuable comments. Thank you very much.

Okawara: Thank you very much everyone for coming, and my apologies for running overtime.