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APAC 2021 Proxy Season Review

Part 2. Japan

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There have been many corporate-governance related topics in the Japan market in 2021, seen against the backdrop of global warming and 2050 targets for national carbon neutrality. Firstly, the Corporate Governance Code was revised in June. Meanwhile, the reorganization of the Tokyo Stock Exchange (TSE) made it clear that companies listed on the top-tier Prime Market would be required to have high stock liquidity and a greater level of corporate-governance code standards. Lastly, shareholder proposals were submitted to some Japanese companies to strengthen Environmental, Social, and Governance (ESG) disclosure, in-line with growing global demand for such initiatives.

In this review we will explore policy trends, investor actions and key dissent in resolutions in Japan. A follow-up report will focus on developments in South Korea market.

2021 Voting Policy Trends

Voting advisory firm Glass Lewis introduced new guidelines regarding cross shareholdings this year.[1] Glass Lewis will generally recommend voting against the chair of the company (or the most senior executive in the absence of a company chair) when the size of strategic shares held by the company exceeds 10% or more of company's net assets in the securities report disclosed in the previous fiscal year. Institutional Shareholder Services (ISS) announced it plans to introduce similar guidelines on cross shareholdings starting in February 2022.[2] At companies with a statutory auditor structure, ISS might consider voting against when top executive(s) allocates a significant portion (20 percent or more) of its net assets to cross-shareholdings.

Moreover, if the board, after the shareholder meeting, will not include at least two outside directors, and at least one-third of the board members will not be outside directors, they can consider opposing the resolution. Multiple major institutional investors raised similar criteria (one-third or more) since the last year. It appears that few of them will change the criteria significantly in the current fiscal year. Stemming from this, according to voting results disclosed by Japanese institutional investors by the end of August (Table 1), the ratio of votes against company proposals decreased slightly compared to last year.

Table 1: Institutional investors' opposing votes on resolutions proposed from company

Institutional Investor	2019	2020	2021
Asset Management One	14.8%	14.7%	14.3%
Sumitomo Mitsui Trust Asset Management	19.4%	20.1%	16.9%
Mitsubishi UFJ Trust and Banking	16.1%	28.3%	23.2%
Resona Asset Management	10.8%	9.8%	11.7%
Nomura Asset Management	8.0%	7.7%	8.1%
Daiwa Asset Management	10.4%	10.6%	7.8%
Nikko Asset Management	15.5%	12.0%	12.4%
Mitsubishi UFJ Kokusai Asset Management	13.9%	17.4%	15.4%
Nissay Asset Management	11.1%	9.7%	11.2%
Sumitomo Mitsui DS Asset Management	30.2%	24.8%	22.3%
BlackRock Japan	5.4%	6.1%	6.4%
J.P. Morgan Asset Management	21.4%	21.8%	18.8%
Fidelity Investment Limited	9.0%	7.9%	6.2%

From IHS Markit's internal data

[1] Glass Lewis 2021 Proxy Guidelines

[2] PROPOSED ISS BENCHMARK POLICY CHANGES FOR 2022

Revised Corporate Governance Code

On 11 June 2021, TSE and the Financial Service Agency (FSA) revised the Corporate Governance Code. The main points in the revision were:

- Enhancing independence and promoting board diversity
  - Increase number of independent directors to at least one-third of the board for Prime-Market-listed companies
  - Establish a nomination committee and a remuneration committee
  - Disclose a skill matrix of board members conforming to a company's business strategy
  - Appoint independent directors having managerial experiences at other companies
  - Disclose a policy and voluntary measurable targets to promote diversity in senior management by appointing females, non-Japanese, and mid-career professionals
  - Disclose human-resource-development policies ensuring diversity, including status of implementation
- Emphasis on ESG
  - Develop a basic policy on sustainability and disclose ESG initiatives
  - Enhance climate-related disclosure based on Task Force on Climate-related Financial Disclosures (TCFD) recommendations, or equivalent international frameworks, at Prime- Market-listed companies
- Other changes to protect shareholder rights
  - Appoint more independent directors to form majority of boards or establish an independent special committee to cope with conflicts of interest between parent companies and minority shareholders
  - Promote the use of electronic-voting platforms and disclosures in English

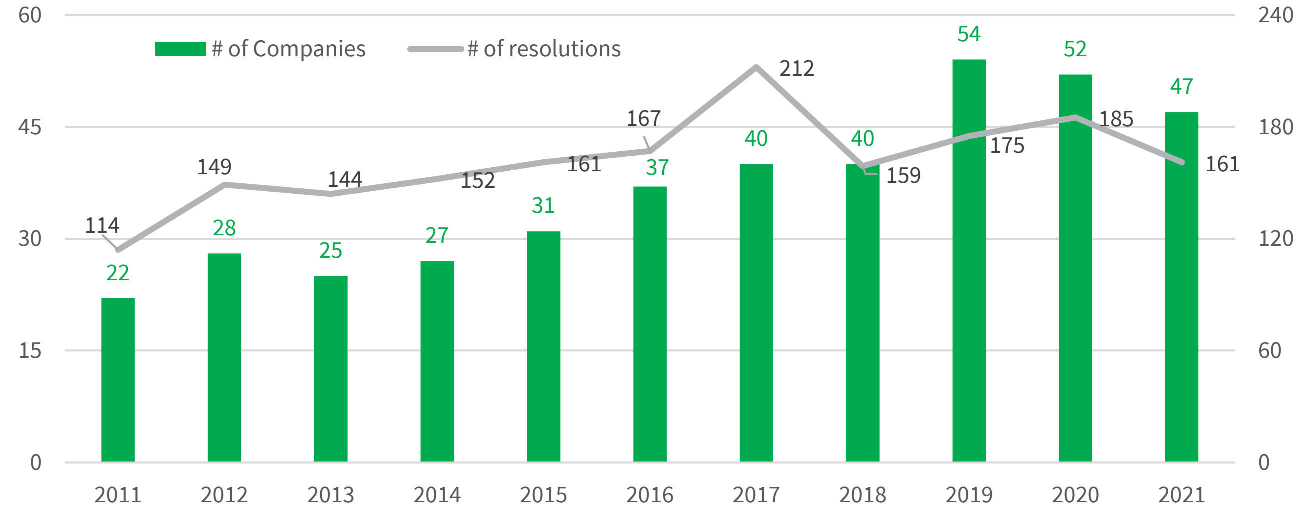
The revisions reflected focus on diversity and independence of board, extending to gender diversity, nationality, and professionalism. It was recommended that issuers concentrate on their board status, ESG strategy, and company disclosure. It was notable that the codes emphasized ESG disclosures such as TCFD.

In line with the revised Corporate Governance Code, corporates are therefore in need of disclosing more in-depth and transparent information for shareholders and market participants. Board skill matrix for example, could be a good practice for companies for better ESG implementation in disclosure strategy. However, for these best practices to become a norm, active participation including other market participant such as regulatory institutions, working groups is needed.

Shareholders and ESG related resolutions

Shareholder activism has been increasing in the Japanese market over the past few years and the number of shareholder proposals at June 2021 meetings remained high (Graph 1). In 2021, the number of shareholder proposals requesting shareholder returns increased, surpassing the total number of proposals for the election and removal of directors, which were highest in last year's tally. Other notable increase was in ESG-related shareholder proposals, which rose from 1.1% to 5.0% of all shareholder proposals. Among these, the proposals that received 10% support are the four proposals in Table 2.

Graph 1: Number of companies and resolutions of shareholder proposals



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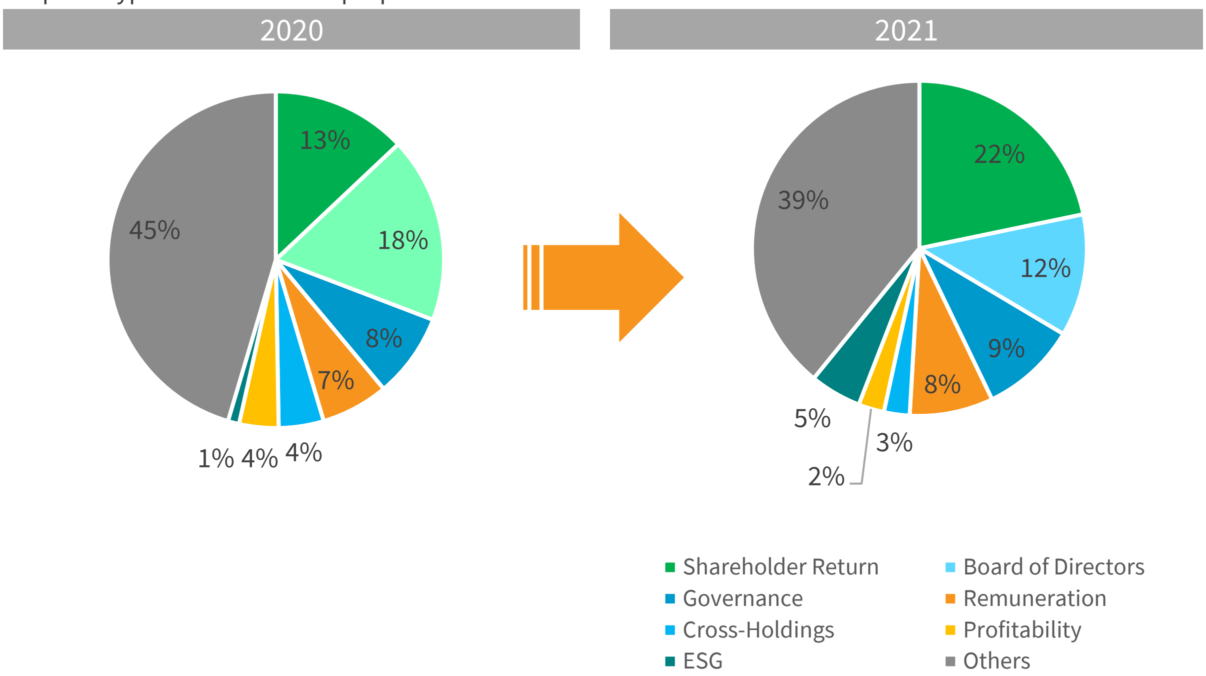
Graph 2: Types of shareholder proposals



Most of the "others" are anti-nuclear-power-related shareholder proposals submitted to electric power companies.
From IHS Markit's internal data

Table 2: ESG-related resolutions with high approval rates (by the end of June 2021)

Ticker	Company	Resolutions	Proposer	For (%)
8306	Mitsubishi UFJ Financial Group	Regarding Aligning Business Strategy to the Paris Agreement	Kiko Network	22.7%
8053	Sumitomo Corp.	Regarding Reporting on Paris-aligned Targets for Coal, Oil, and Gas Assets	Market Force	20.0%
9503	Kansai Electric Power Co. Inc.	Regarding Decarbonization of Power Generation Business	Kyoto City	18.4%
5901	Toyo Seikan Group Holdings Ltd	Regarding TCFD Reporting	Oasis Investments II Master Fund Ltd.	14.4%

From IHS Markit's internal data

Case study: MUFG

The shareholder proposal for Mitsubishi UFJ Financial Group (MUFG) receiving the most favorable votes in Table 2 attracted a lot of attention. Proposer Kiko Network submitted a similar measure to Mizuho Financial Group, Inc. in 2020. That proposal was rejected, but received more than 30% support. With interest in ESG on the rise, there was much interest surrounding the recipients and reception of Kiko Network shareholder proposals this year.

However, only some 22% of shareholder proposals were submitted to MUFG, which was lower than the percentage of support at Mizuho. This was mainly due to the fact that two major voting advisory firms evaluated ESG-related initiatives at MUFG and recommended against the shareholder proposal. On the other hand, several Japanese institutional investors voted in favor of the proposal after voting against it last year. Among overseas institutional investors, some institutions that prioritize their own standards over those of advisory firms supported the proposal. Although the approval rate declined due to recommendations by advisory firms, it is highly likely that the number of shareholders supporting ESG-related proposals increased this year, especially among institutions that make their own exercise decisions.

Case study: Toshiba

The decision to hold the Toshiba Corp. shareholder meeting was influenced by the report of a third-party committee released on 10 June 2021. This committee was created at the extraordinary shareholders' meeting in March 2021 to investigate whether the vote counting for the July 2020 shareholders' meeting had been properly conducted. In its report, the committee concluded that Toshiba, in cooperation with Ministry of Economy, Trade and Industry (METI), exerted pressure on the exercise behavior of overseas institutional investors and the meeting was not conducted fairly.

In response to the report, Toshiba announced the resignation of two of its nominees for the 2021 board. In addition to these resignations, Mr. Osamu Nagayama, a member of the board, and Mr. Nobuyuki Kobayashi, a member of the audit committee, were not approved, resulting in only nine of the original 13 nominees receiving approval. In addition, George Olcott, one of the approved directors, announced his resignation in protest of the rejection of Nagayama, who was to play a key role in restructuring, leaving only eight directors after the annual meeting.

In fact some institutional investors supported Nagayama's leadership, many investors took seriously the fact that he was deemed inappropriate in the report’s findings and voted against the proposal. However, it seems many investors also took seriously the fact that the board and nomination committee were rated inappropriate and exercised their opposition.

Conclusion

In conclusion, with the exception of a few cases such as Toshiba, the number of ESG-related shareholder proposals increased, but the rate of approval was not as high as expected. With the revision of voting standards for institutional investors taking a break, the opposition rate to company proposals generally declined due to efforts by issuers to improve governance.

However, as mentioned, from the 2022 annual general meeting, ISS will raise the ratio of outside directors for companies with a statutory-auditor structure. It will also introduce a new policy regarding cross shareholdings. On the other hand, companies are expected to sell cross shareholdings and disclose more TCFDs in-line with the revised Corporate Governance Code in order to be listed on the Prime Market. We can also expect shareholder activism to accelerate and promote this trend. This year's calm may just be a prelude to further governance improvements in the future.

Authors

Atsushi Matsunaga
Director, Strategic Governance and ESG Integration Advisory
Atsushi.Matsunaga@ihsmarkit.com

Mr. Matsunaga focuses on analyzing and advising APAC and Japanese issuers on governance risks leading up to contentious proxy campaign situations through an ESG, M&A, and governance lens.

He has over 20 years of experience in the corporate governance advisory service industry of Japan. Prior to joining IHS Markit in Summer 2020, Mr. Matsunaga spent 12 years as a corporate governance consultant including board evaluations and the proxy voting simulation at IR Japan. Before that, he had provided IR consulting services at IR Japan. Mr. Matsunaga earned his bachelor's degree in Economics at Meiji Gakuin. He is a CMA (Certified Member Analyst of the Securities Analysts Association of Japan) charterholder. Mr. Matsunaga worked with some clients on proxy businesses, such as Nomura Holdings (JPN), Sanrio (JPN) , Tsukasa Corporation (JPN) and LG Chem (KOR).

Yura Ahn
Senior Associate, Strategic Governance and ESG Integration Advisory
Yura.Ahn@ihsmarkit.com

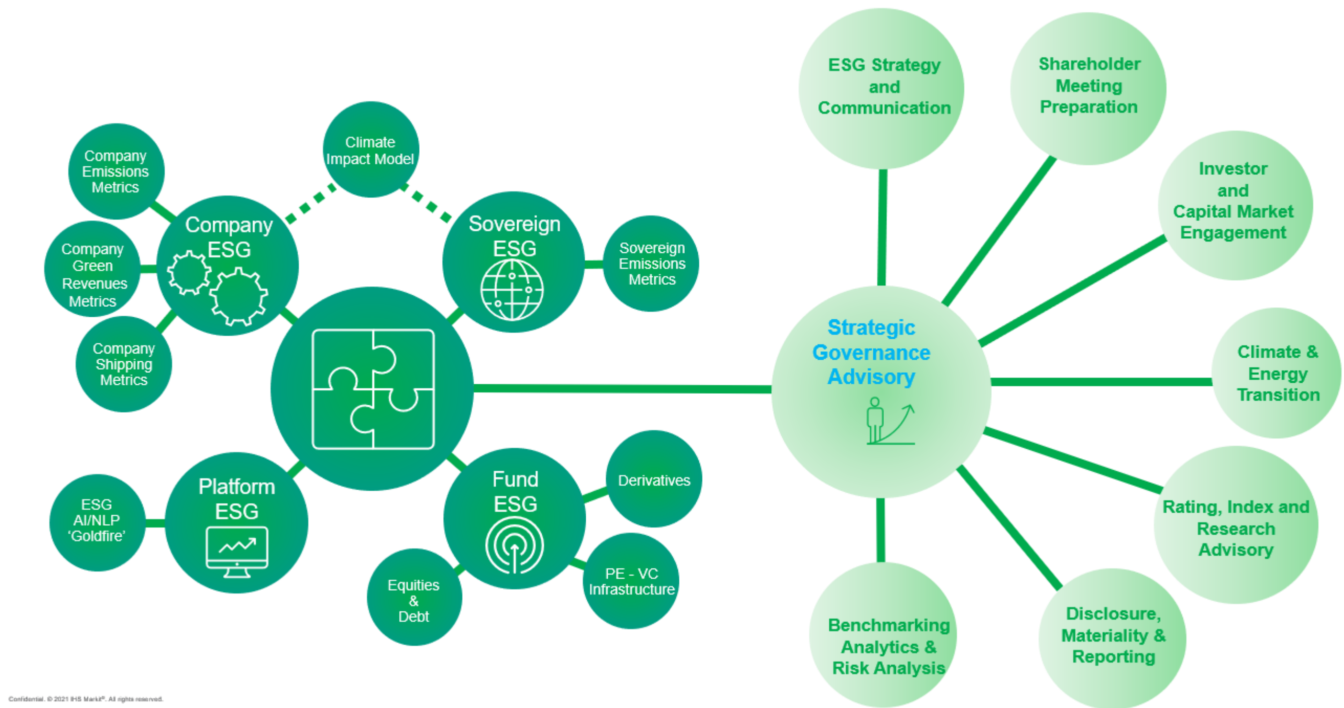
Ms. Ahn joined IHS Markit ESG, M&A and Corporate Governance Advisory Team in 2020 and is part of global Issuer Solutions team. She is currently guiding Korean and other APAC based client issuers to successfully prepare and host shareholder meetings, mitigating any possible risks in communication with shareholders and other stakeholders. She also has experience of managing proxy solicitation projects, engaging with proxy advisory firms and foreign institutional investors. Prior to joining IHS Markit, she worked as ESG analyst in Korea Corporate Governance Service (KCGS) based in Seoul, specializing in Responsible Investment Analysis and Proxy Advisory for buy-side. Her main role was to analyze corporate governance risks of listed companies and guide asset owners and managers on shareholder engagement. She also provided proxy advisory service to asset owners including National Pension Service (NPS) and Korea Post. She has experience and knowledge on investment stewardship as she worked in Korea Stewardship Center, supporting the establishment of Korea Stewardship Code.

How IHS Markit can add value…

Our advisory program helps companies position themselves to benefit from the growing ESG-linked capital pool and proactively prepare for the regulatory, reporting and industry trends that are relevant to each business. Our global team advises at board and management level as well as with investor relations, communications, and sustainability teams.

Our team will tailor the solutions so that companies can:

- Analyze top investors' ESG DNA
- Target existing and potential ESG-focused investors
- Advise, plan, and facilitate investor engagement on ESG issues
- Assess capital market sentiment
- Understand the influence of a particular ESG rating and disclosure framework
- Implement a climate transition program in line with carbon neutral scenario



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CUSTOMER CARE

NORTH AND SOUTH AMERICA

T +1 800 447 2273
+1 303 858 6187 (Outside US/Canada)

EUROPE, MIDDLE EAST AND AFRICA

T +44(0) 134 432 8300

ASIA PACIFIC

T +604 291 3600

JAPAN

T +81 3 6262 1887

E CustomerCare@ihsmarkit.com

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