Japan Losing Patience With Ghosts Lingering in the Boardroom

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For as far back as people can remember, they've been there in boardrooms across Japan, the lingering ghosts of past regimes.

They're the former presidents and executives who stick around for years in adviser roles after their stint at the top has finished. Old men -- usually -- with no legal responsibility but plenty of power, they've long been criticized for getting in the way of incumbent management teams.

All of a sudden, their presence is being questioned anew as the nation overhauls its corporate governance structures. The trade ministry -- credited with masterminding the high-growth era until the 1980s -- has started an investigation. An influential proxy **adviser** plans to urge clients to vote against company attempts to introduce the system, and the man tasked with suggesting what's **next** for Japan's firms says it's time advisers stepped down.

"These advisers should quit," said Kazuhito Ikeo, a professor at Tokyo's prestigious Keio University and head of the state panel that's assessing the effectiveness of the country's sweeping governance revamp.

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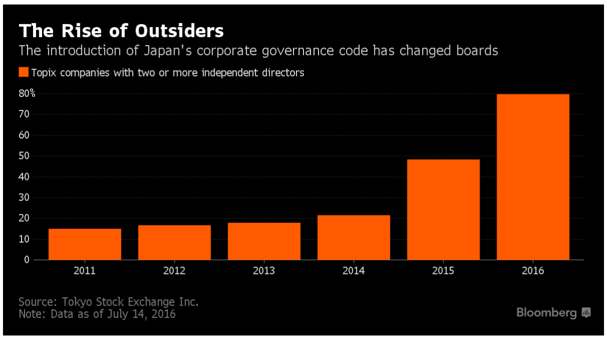
Japan rewrote its rules for companies and investors under Prime Minister Shinzo Abe, aiming to make executives use cash hoards better for generating profits. Since a corporate governance **code** introduced last year, firms must appoint two independent directors or explain why they didn't. About half the companies on the Tokyo Stock Exchange's main board now **meet** the requirement.

For a QuickTake on Japan's corporate governance reforms, click here.

But this has thrown up some unintended consequences. For one, some firms say there's a shortage of suitable candidates. Some 117 outside directors or auditors sat on four or more boards at the end of August, according to Nomura Holdings Inc. And that's the main reason Professor Ikeo has his sights on the adviser system. Getting rid of it would free up a pool of experienced people, he said.



"I call them the ghosts of the boardroom," said Nicholas Benes, the Tokyo-based head of the Board Director Training Institute of Japan. "Almost every industry has a lot of these guys. The really disturbing thing is you don't even know how many there are."

'Pension System'

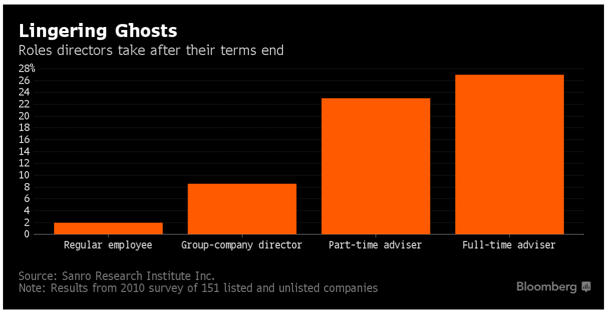
Benes says that getting an adviser position is almost automatic for retiring directors at Japanese firms, and the roles can last for five years. It's like a pension system, a built-in benefit of serving on the board, he said. While advisers exist in other markets such as the U.S., it's usually a short-term posting given to the chief executive officer or chief financial officer while they see out their non-compete clauses.

The problem in Japan, he says, is many advisers have a harmful influence on company strategy, because they're more concerned about protecting their legacies than suggesting what's best. Incumbent boards would be reluctant, for example, to sell a loss-making non-core subsidiary if it had originally been bought by one of the advisers, he said.

"When people retire, they should retire," said Jamie Allen, secretary general of the Asian Corporate Governance Association in Hong Kong. "I don't think the board can be considered to be functioning properly when the former CEO or chairman of a company still has influence."

The trade ministry started gathering data on advisers in August by surveying companies on the first and second sections of the Tokyo exchange, according to an official who asked not to be named, citing ministry policy. It's looking at pay, responsibilities, perks and whether firms have considered scaling back the system. The ministry plans to publish the results by around March before deciding its next move.

Institutional Shareholder Services Inc. is also about to seek public comment on Japan policy changes including telling its more than 1,600 clients to vote against amendments to articles of incorporation designed to introduce the adviser system, according to Takeyuki Ishida, head of Japan research.



Some of the biggest firms have already got rid of advisers. Sony Corp. did so in 2006, while Tokyo Electric Power Co. scrapped them in 2012, a year after the nuclear disaster at one of its plants in Fukushima.

The average annual pay in 2010 for full-time and part-time advisers at 151 listed and unlisted companies was 6.8 million yen ($62,000) and 5 million yen, respectively, according to a **survey** by Sanro Research Institute Inc. Yukio Kashio, former CEO of Casio Computer Co., **earned** 1.1 billion yen in his role as special adviser in the year ended March 2014, while Kyoden Co.'s Hiroshi Hashimoto took home 1.3 billion yen that year for serving as the circuit-board maker's chief adviser, according to Tokyo Shoko Research Ltd.

While governance specialists say advisers influence current leadership teams, some companies disagree.

Komatsu Ltd.'s management "is completely handled by the president, chairman and below," said Akira Sato, a spokesman for the maker of construction machinery. "Our adviser never gets involved in internal operations," he said, noting that Komatsu doesn't disclose his salary and has no plans to do so.

Full Disclosure

Still, Benes says the regulator should make firms publicize who has adviser positions and how much they're paid, while Allen says the system is unfair to both existing management teams and shareholders. And for Hiroki Sampei, director of research at Fidelity International in Tokyo, urging outgoing executives to become outside directors elsewhere instead would kill two birds

"It looks from the outside like the president is in control, but actually there are other leaders in the shadows," he said. Scrapping the system would "stop abdicating emperors from retaining power."

(Corrects Sampei's company name in second-to-last paragraph.)