Chizema, A., & Shinozawa, Y. (2012). "The 'Company with Committees': Change or Continuity in Japanese Corporate Governance?", *Journal of Management Studies*, 49(1), 77-101.

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The Adoption of the Board Committee System

■ Questions

Q1: Discuss briefly the **core argument** of this work.

Q2: Distinguish **Japan's statutory auditor system** from **its new committee system**.

Q3: Explain the **logic of adopting the board committee system** (*i.e.*, nomination, audit, & remuneration committees).

Q4: Clarify **each hypothesis** with your own words **theoretically**.

Q5: Interpret the results indicating **what factors** determine the likelihood of **adopting the committee system**.

Q6: What is the **take-home message** based on the findings?

The Adoption of the Board Committee System

■ The Core Argument of This Article

❖ Research Goal

– What determines the adoption of the committee-based governance system (*i.e.*, audit, nomination, & remuneration)?

❖ Why Important?

1. This study enriches the debate on the **diffusion** of specific **shareholder-oriented management practices** (*i.e.*, the committee system) across national corporate governance systems.
2. **No scholarly attention** has been directed to the **dynamics or determinants** of adopting the **committee system**.
3. The authors focuses on **corporate governance changes** in **Japan** that experiences **a conflict** between **global capital market forces** of change & deeply embedded **institutional practices of continuity**.

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Institutional Theory

- **Institutions** are defined as **both formal & informal rules** that **constrain human interaction** in a society (North, 1991).
- … provide **a framework for social interaction** & make **social order** possible by **reducing uncertainty** (Scott, 2001).
- … are social structures that are composed of **cognitive**, **normative**, & **regulative** elements (Scott, 2001).
- Institutions, including **corporate governance institutions**, tend to reinforce the continuity of established systems, behavior, & practices (Chizema & Shinozawa, 2012).
- Corporate governance institutions **change from time to time** (Fiss & Zajac, 2006) due to both **internal & external pressures** (Oliver, 1992).

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Dimensions of Institutions

Degree of Formality	Examples	Supportive Pillars
1 **Formal institutions**	> Laws > Regulations > Rules	> Regulatory (coercive)
2 **Informal institutions**	> Norms > Cultures > Traditions > Ethics	> Normative > Cognitive

The institutional framework governing a particular context

Key Points

- **Globalization-driven changes** may **not** be **uniform** even **within the same country** (Chizema, 2008).
- **Japan** is a country with **deeply rooted traditions of business practices**.

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■ ‘3’ Types of Institutional Isomorphism

❖ *Coercive Isomorphism*

– … is driven by **pressures from other organizations** on which a focal organization depends & by **pressures to conform to the cultural expectations of society at large**.

❖ *Normative Isomorphism*

– … is traditionally a result of **professionalization**, where **members of professions** receive **similar training** & interact through **professional bodies**.

❖ *Mimetic Isomorphism*

– … is **a response to uncertainty**. In situations where a clear course of action is unavailable, managers may **imitate a peer organization perceived to be successful**.

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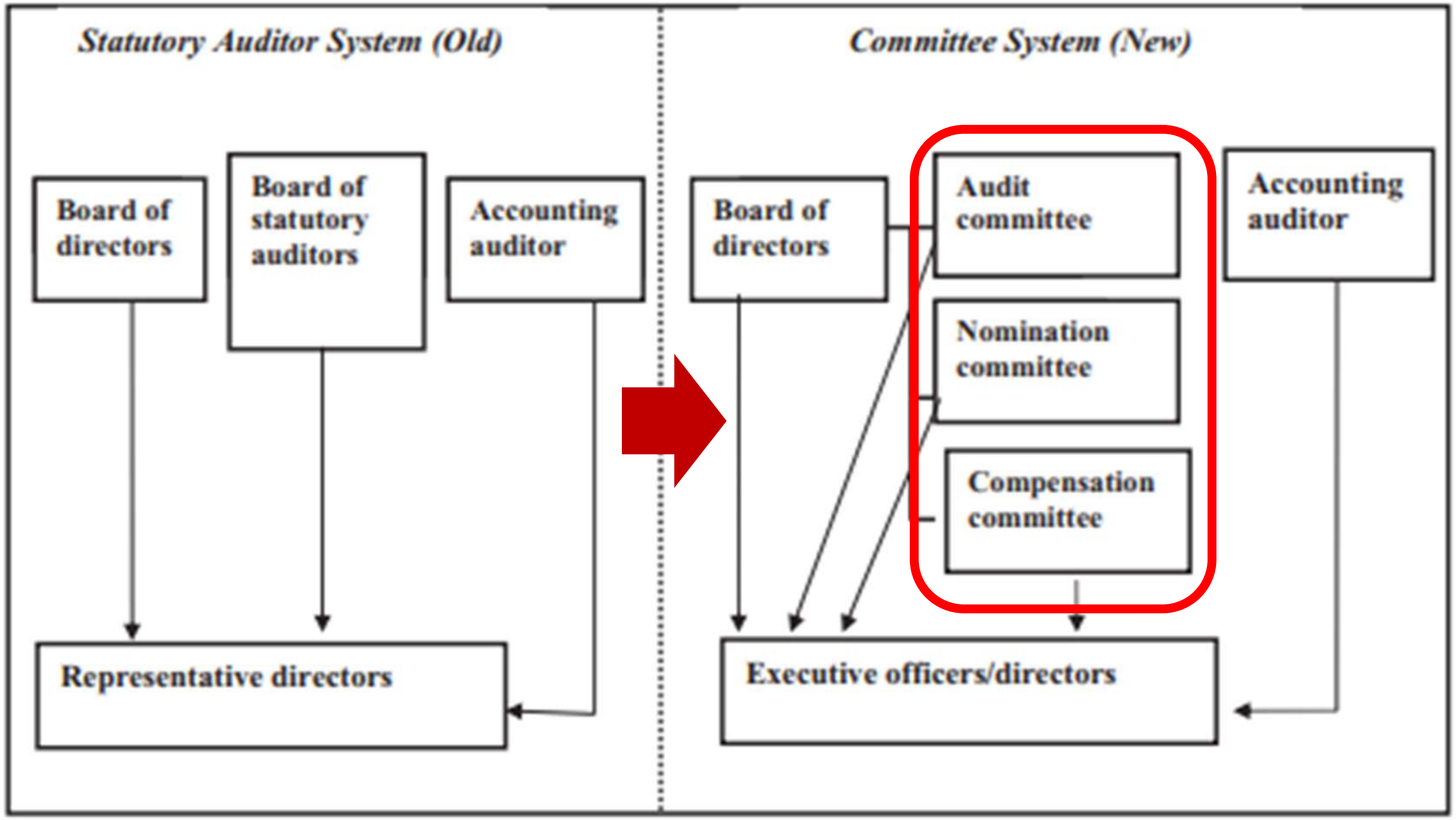
■ The Old & New Board System in Japan



❖ In the **committee system, each committee** must have at least **3 directors**, a **majority** of whom must be **outside directors**.

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■ '3' Committees

❖ *The Audit Committee*

– … has **powers & duties** to **monitor directors & executive officers** in the **performance of their duties**, as well as **the right to propose** the appointment or dismissal, or to refuse reappointment.

❖ *The Nomination Committee*

– … is responsible for **determining any proposal for the election or removal of directors**, which must be adopted by shareholders at the general meeting.

❖ *The Compensation Committee*

– … decides on policy regarding the **content of compensation** & related matters **for directors & executive managing directors**.

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Data

❖ *Adoption & non-adoption of the committee system*

Year	*Adopting firms (cumulative)*	*Non-adopting firms*
2002	00	235
2003	14	221
2004	18	217
2005	18	217
2006	19	216
2007	19	216
2008	20	215
2009	20	215

❖ Roughly **9%** of the sampled firms **adopted** the **board committee system**.

The Adoption of the Board Committee System

Data

❖ *T-test for committee-adopting & non-adopting firms*

	Mean		
	Adopters	*Non-adopters*	*Difference*
Cross listing	0.20	0.05	0.15**
Financial performance	3.19	6.12	−2.93
Firm age	65.40	63.86	1.54
Cross holdings	23.90	10.61	13.29***
Foreign ownership	27.10	20.72	6.38**
Bank ownership	31.75	36.65	−4.90**
Employee ownership	1.09	2.34	−0.44
Firm size	20.25	19.87	0.38

❖ The **mean difference** for **cross holdings** shows **highly statistical significance.**

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Advantages & Disadvantages of the Committee System

Benefits

- **Trust from Foreign Investors**
  - In **Europe** & the **USA**, companies with the committee system are perceived to have **higher management transparency & accountability**.
- **Better Corporate Governance**
  - Unlike ordinary corporate auditors, the majority of the members are **outside directors** in each committee, help **manage** the company more **appropriately**.

Costs

- **Difficult to Secure Personnel**
  - Increasing the number of outside directors results in revitalizing discussions. But it can be **difficult to secure the right people** who are familiar with management & the company's business.
- **Increased Reward Burden**
  - Companies with the committee system have **more officers**.
  - **The number of officers (↑)** = the **compensation (↑)**.

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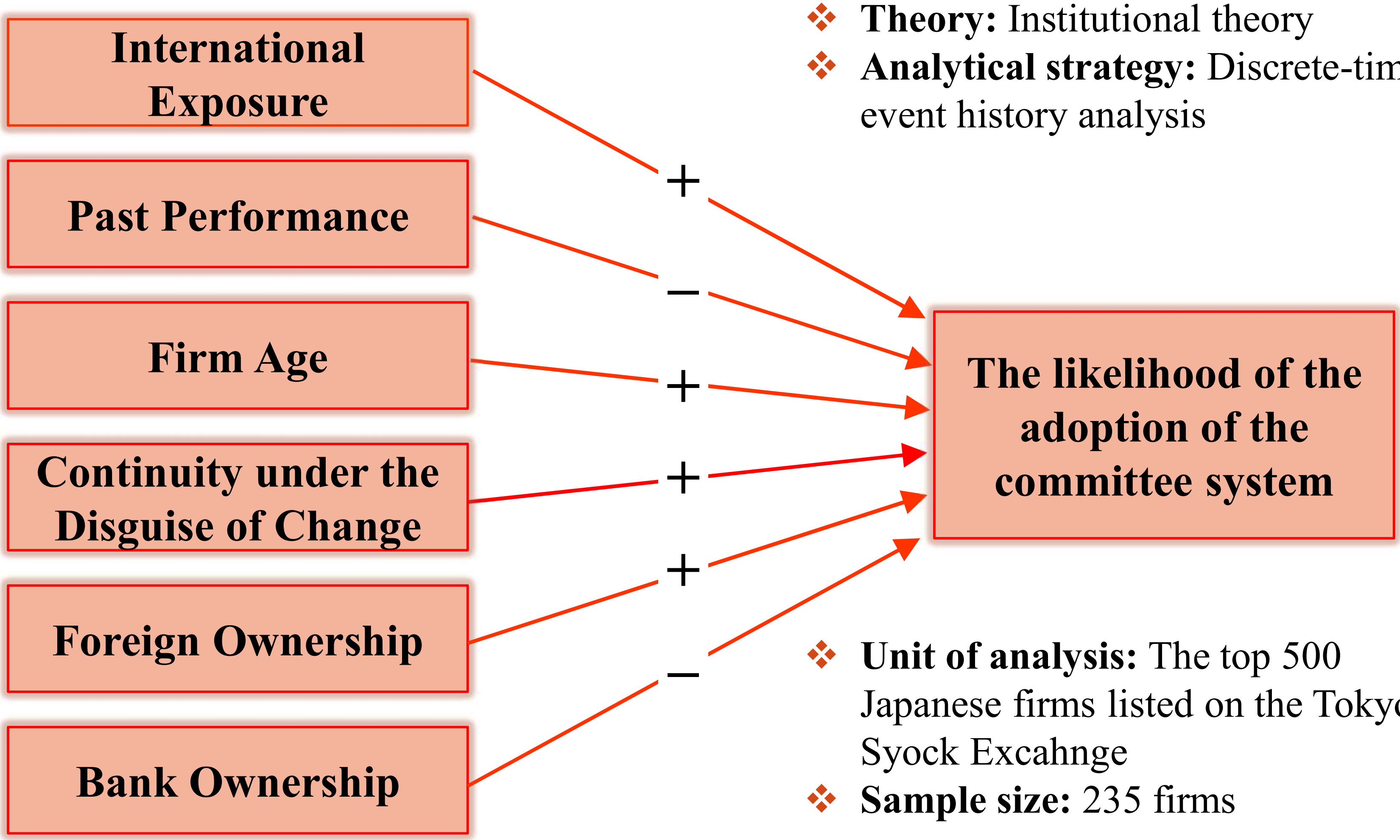
■ Proposed Conceptual Model



- **Theory:** Institutional theory
- **Analytical strategy:** Discrete-time event history analysis

- **Unit of analysis:** The top 500 Japanese firms listed on the Tokyo Syock Excahnge
- **Sample size:** 235 firms

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Hypothesis 1 (Cross Listing)

‘*Firms that diversify their* ***operations into other sectors or in different countries*** *are likely to be exposed to* ***alternative organizational customs***’ (Oliver, 1992: 577).

International Exposure

+

The likelihood of the adoption of the committee system

- The convergence thesis argues the ***gradual erosion of institutional differences*** among different national economies due to ***intensified global competition*** (Deeg & Jackson, 2007).
- Firms that are ***internationally exposed*** through product & financial markets have the chance to ***learn management practices from their customers & competitors*** drawn from alternative models (Chizema & Shinozawa, 2012).
- By listing ***American Depositary Receipts (ADRs)*** in the **USA**, Japanese firms submit themselves to some scrutiny & compliance by the ***Securities Exchange Commission (SEC)***.

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■ Hypothesis 2 (Prior Performance)

Since ***organizational change*** is ***a risky decision***, managers must have ***legitimate reasons & compelling incentives*** to ***break their exisiting routines or practices*** (Greve, 1998).

Past Performance → – → **The likelihood of the adoption of the committee system**

- ***Poor performance*** provides ***a strong incentive*** for firms to ***look for new ways to improve*** (Miller & Chen, 1994).
- ***Poor past performance*** reflects the ***ineffectiveness of existing practices*** & provides strong & legitimate reasons for firms to ***reform their administrative systems***.
- Where ***a firm's performance is weak*** (*i.e.*, share price falls or rates of job creation are low), organizational groups may express their dissatisfaction by ***bending the balance of forces in favor of institutional change***.

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Hypothesis 3 (Firm Age)

- ***Firm age*** may be indicative of ***experience-based capabilities***, ability to adapt, reliability, & market credibility (Baum & Shiplov, 2006).

- ***With age***, a firm may ***develop capabilitie to undertake change & adapt to new environments*** (Kelly & Amburgey, 1991).

Firm Age → + → **The likelihood of the adoption of the committee system**

- ***Older firms*** have greater ability & flexibility to adopt a new form of committee governance than younger firms due to their ***legitimacy with supporting institutions***.

- Supporting institutions could include consultancy firms, the institute of directors, & professional accounting bodies. ***Age*** reflects experience & the level of ***the firm's relationships with supporting institutions***.

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■ Hypothesis 4 (Cross Holdings)

- The *concept* of *outside directors* in *Japan* is *different* from that of the *American model* of corporate governance (where they are independent).

- At least, ***2 outside directors*** are needed to serve on ***each*** of the ***3 committees*** (i.e., not easy to find them).

- All of the outside directors of the ***Hitachi group companies*** are ***affiliated*** with ***Hitachi Ltd***., & most of the outside directors of the ***Nomura subsidiaries*** are ***affiliated*** with ***Nomura Holdings*** or ***Nomura securities*** (Yamada, 2003).

Continuity under the Disguise of Change — + → **The likelihood of the adoption of the committee system**

- ***Cross holding firms*** can ***appoint individuals*** who may ***not threaten to change the status quo***. By appointing ***outside directors*** from their ***affiliated & sibling companies, parent companies can maintain gerater control over member firms*** (Gilson & Milhaupt, 2005).

- ***Corporate governance changes*** may be ***cosmetic***, ***simbolic***, or ***camouflaged*** (Buck & Shahrim, 2005) while adopting the committee system.

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■ Hypothesis 5a (Foreign Ownership)

- In ***Japanese corporations***, ***foreign shareholders*** tend to be predominantly ***institutional investors*** from the ***USA*** & ***UK*** (David et al., 2006).
- To ***maximize shareholder value***, foreign investors could threaten to ***sell off their shares*** as the ***'exit'*** option (Nooteboom, 1999).
- ***Foreign ownership*** impacts the ***appointment of outside directors*** on Korean boards (Chizema & Kim, 2010) & strategic change, including employment downsizing & asset restructuring (Ahmadjian & Robbins, 2005).

- ***Foreign investors from the USA & UK*** have ***norms & values*** that emphasize the ***maximization of shareholder value*** (Chizema & Kim, 2010) & they ***welcome governance institutions*** deriving from the ***Anglo-American model***.

Foreign Ownership

+

The likelihood of the adoption of the committee system

- Firms are likely to be obliged to ***appease foreign owners*** by ***adopting American-style committee system***.

The Adoption of the Board Committee System

Hypothesis 5b (Bank Ownership)

- ***Japanese banks*** have traditionally played ***an important corporate governance role***, at least compared with the USA or UK (Dore, 2000).
- The committee system is ***a shareholder-oriented governance element*** thus consistent with ***stock market financing of corporations***. Thus such a system ***ruins*** the ***financial & strategic interests of Japanese banks***.
- Through their embedded relationships with firms, ***banks foster their attitudes & interests*** that promote ***continuity*** (Yoshikawa & McGuire, 2008).
- From ***a power perspective***, **banks** have **'voice'** & direct influence through ***ownership*** (David et al., 2006) & ***seats on the board***.

Bank Ownership —(–)→ **The likelihood of the adoption of the committee system**

- Firms that have ***close ties with banks*** may ***resist*** the ***adoption of the committee system*** as a ***signal*** of their ***solidarity*** with the interests of their ***financial partners***.

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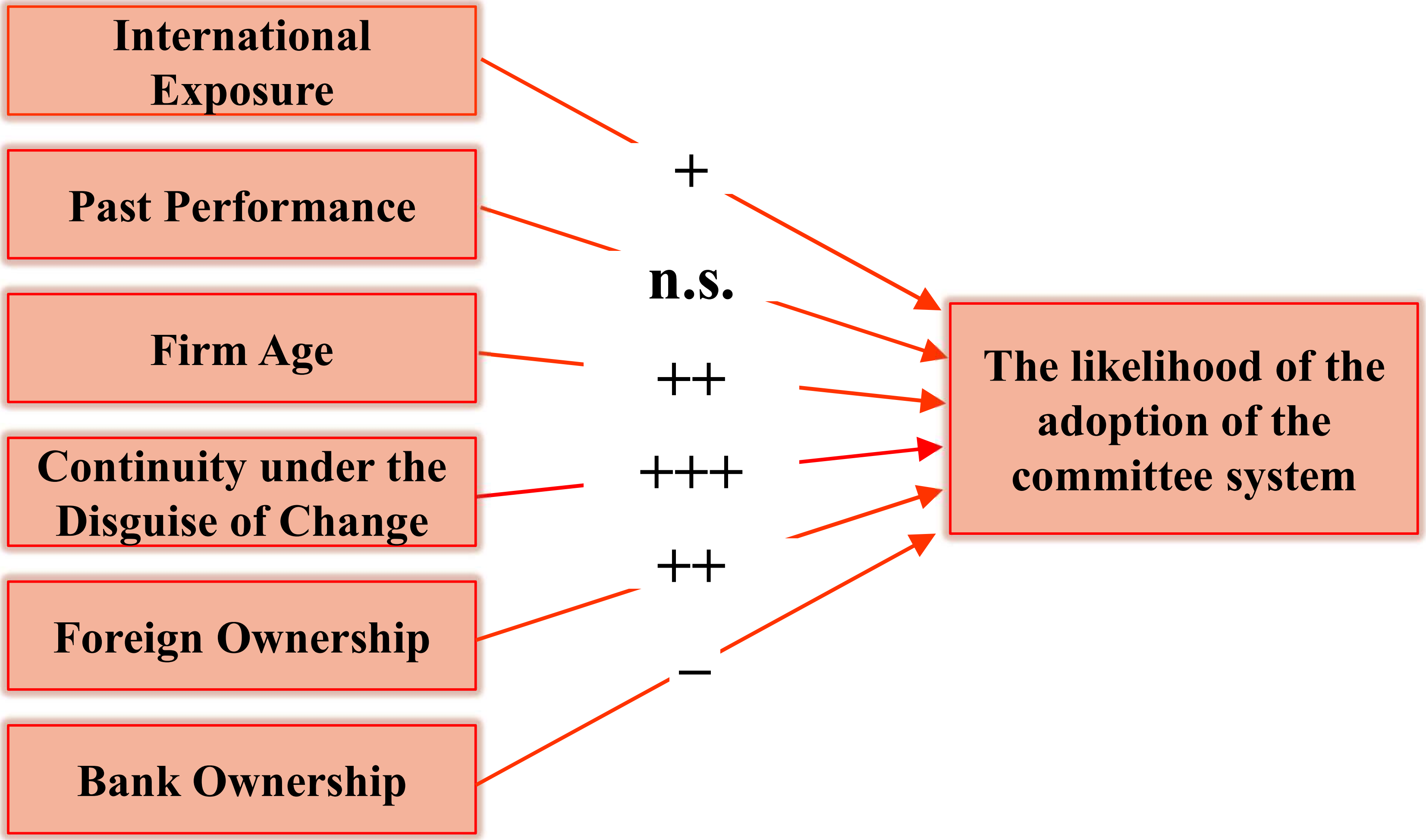
Empirical Results

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
Constant	−8.66 (3.59)	−7.33 (3.51)*	−7.37 (3.47)*	−7.50 (3.49)*	−10.17 (3.64)**	−12.40 (3.90)***	−13.23 (4.04)***	−9.31 (3.93)*
Cross listing		1.27 (0.67)†	1.34 (0.67)*	1.39 (0.69)*	1.79 (0.77)**	1.73 (0.78)*	1.68 (0.81)*	
Financial performance			−0.02 (0.02)	−0.02 (0.02)	−0.02 (0.02)	−0.02 (0.02)†	−0.02 (0.02)	
Firm age				0.01 (0.01)	0.03 (0.01)**	0.03 (0.01)**	0.03 (0.01)*	
Cross holdings					0.05 (0.01)***	0.07 (0.02)***	0.05 (0.02)***	
Foreign ownership						2.85 (1.42)*	3.94 (1.44)**	
Bank ownership						−1.74 (0.82)*	−0.80 (0.79)	
Employee ownership	0.01 (0.04)	0.01 (0.04)	−0.01 (0.04)	−0.01 (0.04)	0.02 (0.04)	0.04 (0.04)	0.02 (0.05)	0.01 (0.05)
Firm size	0.22 (0.22)	0.15 (0.17)	0.15 (0.17)	0.15 (0.17)	0.16 (0.18)	0.27 (0.19)	0.26 (0.19)	0.20 (0.19)
Pre-2005							2.45 (0.54)***	
Post-2005							0.00 (1.38)	
Cross listing × Pre-2005								2.11 (0.92)*
Financial performance × Pre-2005								−0.02 (0.32)
Firm age × Pre-2005								0.03 (0.01)***
Cross holdings × Pre-2005								0.06 (0.02)***
Foreign ownership × Pre-2005								−1.20 (0.79)
Bank ownership × Pre-2005								−0.49 (0.87)
Chi-square	1.61	2.82†	1.48	0.12	16.29***	7.96***	23.12***	51.74***
−2log likelihood	211.93	209.11	207.63	207.51	191.22	183.26	160.13	160.2
Nagelkeke R-square	0.01	0.02	0.03	0.03	0.11	0.15	0.27	0.26

Notes: † $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$. N = 235.

The Adoption of the Board Committee System

Empirical Results



The Adoption of the Board Committee System

■ Conclusive Remarks

❖ Discussions

- This study supports the validity of the **institutional inertia or change perspective** in the context of adopting the committee system.
- Japanese firms with **greater international exposure** (+) tend to adopt the committee system due to both **coercive** (complying with the SEC regulations) & **mimetic pressures** (imitating US firms).
- **More experienced firms** (+) are more likely to adopt the committee system since they are more capable to change given their experience & established ties.
- Firms with higher proportions of **cross holdings** (+) have the opportunity to **appoint outside directors from related firms** (*i.e.*, continuity under the disguise of change).
- **Foreign ownership** (+) & **bank ownership** (–).

The Adoption of the Board Committee System

■ Conclusive Remarks

❖Suggestions for Practice & Policy

- According to **agency theoretical considerations**, the **committee system strengthens** the **supervisory role** of the board.
- The majority of firms that are **not cross listed** & have **lower levels of foreign ownership** & **large bank ownership** may value **continuity** rather than **change**.
- Creating an environment that encourages further **foreign ownership** & **cross listing on American stock exchanges** may increase the chances of adopting the committee system.
- Overall, the findings claim that **Japanese corporate governance** is **NOT naturally converging** on **Anglo-American stock market capitalism**, at least for now.

Conclusive Remarks

❖Drawbacks

- **Limited generalizability** (Japanese corporate governance is shaped by its path-dependent national culture & unique institutions).

- **Indirect measures** of institutional effects were used.

- The sample of this study is **restricted to listed firms only** (The findings may not apply to **small enterprises** or ‘**born global**’ firms.).

- Future research should consider (1) the **characteristics & level** of **independence** of **outside directors** & (2) the **structure** & **processes** of the **different committees** in Japan.

Aoyama (2007). "Oligopoly & the Structural Paradox of Retail MNCs: An Assessment of Carrefour & Wal-Mart in Japan", *Journal of Economic Geography*, 7: 471-490.

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Failed Cases of Carrefour & Wal-Mart in Japan

■ Question

WHAT mistakes did Carrefour & Wal-Mart make in Japan?

Failed Cases of Carrefour & Wal-Mart in Japan

- **Wal-Mart & Carrefour in the Japanese Market in the Early 2000s.**

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

■ The General Trend of Foreign Food Retailers in Japan

- ❖ **Small-scale operations**: CostCo (US, 1999, 5 stores) & Metro (Germany, joint venture with Marubeni Trading, 2002, 3 stores).
- ❖ **New rivals**: 99-yen grocery stores, 100-yen stores, electronics stores.
- ❖ **Divestments of retail MNCs** from Japan: Sports Authority (USA, 96), Footlocker (USA, 97-00), Warner Studio Store (USA, 96-00) & JC Penny (USA, 98-99).
- ❖ **Daily Farm**, a successful HK retailer, set up a JV with Seiyu & opened 4 stores in Japan, was forced into closure due to poor sales in 1998 due to the **lack of competitiveness** in fresh food items unattractive store & poor shelf design.
- ❖ **Carrefour & Wal-Mart** in Japan: **Delivering lower prices**.

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

General Information

Carrefour Japan

- **8 stores** in Japan starting **2000**.
- Wholly-owned subsidiaries (**WOS**).
- Carrefour's overseas expansion to seek out **partnerships with local firms** & to acquire **market-specific knowledge**.
- **13 stores** by the end of 2003.
- The first store in a **Tokyo suburb** of Makuhari in December 2000.
- A "**ghost-town**" in an early afternoon of a weekday.
- The **inability of securing a buyer**.
- 3 stores in the **Tokyo** region & 5 stores in the **Osaka** region were sold to Aeon.

Source: Aoyama,(2007).

Wal-Mart Japan

- **Alliance** with Sumitomo Trading & purchased a 34% share of **Seiyu** (2002) ➔ **50.1% (2005) & 66.7% (2007)**.
- **No visible changes** in storefront design & product variety due to Seiyu's name recognition among Japanese consumers.
- **Voluntary early retirement** of **25%** of its **full-time employees** & raising the **share of part-time employees to 85%**.
- However, the **lay-off** reportedly had **negative impacts** on the moral of Seiyu employees.

Failed Cases of Carrefour & Wal-Mart in Japan

■ Mistakes?

- ❖**WHAT** explains the problems of retail MNCs in Japan?
  - ➢**Key points:** (1) **operational efficiency** & (2) **branding**.
- ❖In the supermarket category, the most common strategy employed among foreign retailers is **low price**.
- ❖**Low-price-strategies** of foreign retailers have been **criticized as unsuitable** for the Japanese market.
- ❖**WHY** did Japanese consumers **NOT** flock to their stores?

  (1) Carrefour & **Wal-Mart** focused on the **low-price strategy** in spite of **the relatively small share of low-income households in Japan** & **a small market for low-end products**. (**Japan: low inequality**)

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

■ Mistakes (Operational Efficiency)

❖ **WHY** did Japanese consumers **NOT** flock to their stores?

(2) The **attitude** of the **Japanese consumers** toward price is particularly **complex**. ➔ Relatively **price-insensitive**. Wal-Mart was keen on introducing its trade-mark **"ever-day-low-price" strategy** at its Seiyu stores with much fanfare. A typical Japanese grocery shopper closely examines **several flyers** of nearby supermarkets & identifies **frequently changing sales items**, & switches where to shop daily. Consumer finds it more economical to continue with the **practice of price comparisons** & **switching places to shop** on the daily basis.

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

■ Mistakes (Operational Efficiency)

❖ **WHY** did Japanese consumers **NOT** flock to their stores?

(3) Both companies insisted that their strategies for low-cost operations that worked elsewhere would eventually win customers in Japan. They **stacked up high in large quantities on shelves** for visibility & shelf space maximization, but at the expense of store attractiveness. Seiyu's clientele was mainly the **middle-aged & elderly loyal customers** who were NOT impressed with low-cost display of bulk.

(4) Carrefour reportedly insisted on transferring other proven strategies from their home markets. **Store layout** was designed to direct customers to form **a one-way traffic from entrance to exit**. Supermarkets substitute for **'refrigerators' in Japan** ➔ **Lean consumption**.

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

■ Mistakes (Operational Efficiency)

❖ **WHY** did Japanese consumers **NOT** flock to their stores?

(5) **Domestic competitors** employed strategies that went directly against the retail MNC's low-cost approach.

Visibility & **customer appeal**, **great variety** in a vigorous thriving atmosphere. They particularly exhibit particular **sensitivity to seasonal changes** in food items, **awareness to gift giving seasons**, **love new products** & consider **freshness** as extremely important. ➔ For example, merchandise in its fresh seafood section **changed 3 times as a day**; whole fish from nearby ocean in the morning, sliced into sashimi in the afternoon; & marinated & grilled fish in the evening.

Source: Aoyama,(2007).

Failed Cases of Carrefour & Wal-Mart in Japan

■ Mistakes (Branding)

- It is well-acknowledged that the Japanese consumer has been the **'most difficult consumer to strategize'**, as they require **high quality** on everything, & are **knowledgeable** about products, service, quality & prices from around the world.

- **Image gap**: Japanese consumers' previous experience with French retailers was largely shaped by luxury boutiques (*e.g.*, Chanel, Louis Vitton & Hermes).

- Wal-Mart's **low-cost, low-quality approach** was widely blamed for its most recent **poor performance** as it ruined Seiyu's highly profitable apparel section.

Source: Aoyama,(2007).

The End of Today's Lecture

ご清聴有難う御座いました。

Thank you so much!

Vielen Dank für Ihre Aufmerksamkeit!

Grazie mille !

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