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Disclosure pressure ramps up Japanese asset managers' scrutiny at company AGMs

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- 20% vote against a resolution is viewed as a significant protest
- Real test comes when cross shareholders seriously start unwinding
- Corporate disclosure pressure will herald major dissent increase

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Investors have stepped up their scrutiny of some Japanese companies at AGMs by voting against directors who have failed to improve corporate value and in support of proposals designed to enhance shareholder value, asset managers and investors said.

“An increasing number of asset managers voted against directors while supporting shareholder proposals because they are now under pressure to disclose their [own] voting results,” a Tokyo-based asset manager said.

In a highly unusual move, shareholders of **JP Holdings** [TYO:5306], a Japanese nursery service company, succeeded in ousting six directors at the AGM in June by voting against their re-election and in support of two directors recommended by a dissident group holding a 27.4% stake.

The six directors received only 36.06%-49.15% of the votes on average, according to a filing with the Financial Services Agency, while a typical figure for the re-election of directors is 95%-99% in Japan.

A similar incident has occurred only once in the past in Japan. In 2008, shareholders of **Aderans**, a wig maker, ousted the company’s directors by voting against their re-election in line with a proposal submitted by US activist **Steel Partners**.

Activist **Strategic Capital** retracted in late May an AGM proposal that it had submitted to **Shin Nippon Air Technologies** [TYO:1952] after the company announced on 14 May a plan to increase its shareholder returns from 38.5% to 50% over the medium term. This included a dividend hike and a share buyback of up to 10% of its outstanding shares.

The move came in response to the activist’s pressure over the past few years. Strategic Capital has been submitting its proposals to Shin Nippon Air since 2016 and having regular dialogue with the company’s directors.

This year, Strategic Capital negotiated especially closely with the company for a few weeks after submitting a proposal on 24 April that urged the company to increase the return to shareholders to more than 100%.

“Shin Nippon’s payout ratio is 30%. If a share buyback of up to 10% is conducted within two to three years, the return to shareholders will be more than 70%,” said Tsuyoshi Maruki, CEO of Strategic Capital. The share price jumped 16% to hit this year’s high of JPY 1,900 on 14 May in response to the announcement.

Also, it should not come as a surprise that Susumu Kotani, the chairman of **Pioneer** [TYO:6773], secured only 67% of the votes, compared with 78.28% last year, for reappointment at its AGM this month. The car navigation system manufacturer's return on equity has been hovering a dismal minus 6.0%-8.7% over the past two years, compared with 5% ROE recommended by Institutional Shareholders Services (ISS) and most Japanese asset managers.

Similarly, Akira Takeuchi, the chairman of **Mitsubishi Materials** [TYO: 5711], won only 75% of the votes, compared with 95.70% last year, for reappointment at its AGM. Earlier this year, the company reported that employees of three of its subsidiaries had falsified inspection results to make products that did not meet customer specifications.

Kajima [TYO:1812] chairman Mitsuyoshi Nakamura won only 71.63% of the votes for reappointment at its AGM this year, compared with 93.62% the year before last. In March, Japanese prosecutors arrested the contractor’s employees suspected of having rigged a bid involving the Tokyo-Osaka maglev project.

Meanwhile, shareholder proposals calling for partial amendment of the articles of **Narasaki Sangyo** [TYO: 8085] and **Chori** [TYO: 8014] such that they restored shareholder authority to vote on income allocation won 35.9% and 27.4% of the votes, respectively, at their respective AGMs.

Excluding **Toray**'s [TYO:3402] 51% stake in Chori, as many as 64% of minority shareholders supported the shareholder proposal from Strategic Capital. "Chori directors are getting a very clear message from shareholders that they will be held accountable," said Strategic Capital's Maruki.

The only solution to resolve this conflict between Chori's parent company and its minority shareholders is for Chori to submit the same proposal as its own next year, or for Toray to privatize Chori as its 100% subsidiary, Maruki added.

At **Mizuho Financial Group** [TYO:3615] and **Mitsubishi UFJ Financial Group** [TYO:3606], shareholder proposals calling for partial amendment to the articles of incorporation around individual executive compensation disclosure, a separation of roles of chairman of the board and CEO and exercise of voting rights of shares held by cross shareholders received more than 30% of the votes.

There has been an increase in the number of directors receiving votes of at least 20% against their re-election, according to the asset manager. "I consider a 20% vote against a resolution is a significant protest, but company directors may find it safe as long as shareholder dissent would not exceed 50% [which is the threshold]," he said.

"Investors have been traditionally reluctant to vote against individual directors," added the asset manager. "The best strategy to increase shareholder support to more than 50% is for activists and their support groups to hold a stake of more than 30%-40%."

"We learned that shareholders stood up for their rights and better corporate governance," Phillip Meyer, chief operating officer of Hong Kong-based activist **Oasis Management**, said after the activist won 28.57% of the votes for their special dividend proposal at **Alpine Electronics** [TYO:6816]. At the same AGM, Alpine President Nobuhiko Komeya won only 71.33% of the votes, down from 92.61% last year.

The increased agitation by asset managers comes after Japan's Financial Services Agency announced in May last year revisions to the Stewardship Code. Asset managers are now urged to reveal how they vote at a company shareholder meeting and explain if they do not comply with the disclosure recommendation. Prior to this, asset managers were only urged to disclose voting results by resolution in aggregate, but not by individual company.

This year, the FSA revised its corporate governance code urging companies to take a drastic look at their cross shareholdings and clarify plans on the reduction of cross shareholdings.

"It is admirable Japan continues to review, revise and improve its corporate governance framework. It is a continuing theme of transparency and accountability. In many ways, this is what corporate governance boils down to," said Oasis' Meyer.

A real test will be Japanese corporate 'cross' shareholders. The unwinding of cross shareholdings would cause an increasing number of financial institutions and companies to start voting in line with ISS recommendations, the asset manager said.

The question is when Japan will start urging these corporates to disclose their voting results. "If these corporate cross shareholders start unwinding their cross holdings, start voting in line with ISS and if they are urged to disclose their voting results, along with asset managers, there would be a huge increase in dissent votes," the asset manager added.

In the UK, the Investment Association's public register keeps track the number of businesses that received more than a 20% vote against any resolution during its annual general meeting and disclose what measures companies have taken to deal with shareholder dissent, according to the IA.

Under Japan's Corporate Governance Code, companies that received significant shareholder dissent against proposed resolutions are urged to start analyzing causes behind such dissent and consider measures to address the issues, such as having talks with shareholders.

However, Yutaka Suzuki, senior researcher at Daiwa Institute of Research, said Japan does not have a clear definition for 'significant dissent', and even if companies analyze causes of such dissent, they are not required to disclose the results of their analysis.

by Norie Hata in Tokyo