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Managers, Bureaucrats, and Institutional Change in Japan

Studying corporate control in Japan is like landing in the middle of a murder mystery. There is indisputably a corpse: in this case, the takeover protection once provided by long-term shareholders was killed between 1996 and 2005, as shown in Chapter 2. How the corpse died and especially what threat the killer poses to other institutions of the Japanese political economy are hotly contested questions. Some adduce the collapse of cross-shareholdings as a sign of the thoroughgoing liberalization of the market for corporate control, in which western institutional investors now call many of the shots in Japanese companies.[1] Others claim, contrariwise, that the limited number of takeovers to date is proof positive that the Japanese market for corporate control remains closed even without cross-shareholding, and that entrenched managers can protect themselves from any unwanted advances.[2] A third group of scholars sees a new organizational diversity in Japan: some firms play by the rules of an active market for corporate control, while others have tried to rebuild interfirm alliances as a form of protection.[3] As this book goes to press, it is not entirely clear how active the market for Japanese corporate control is in international comparison. While hostile takeovers have rarely succeeded in recent years in Japan, the increasing number of attempted takeovers suggests that the character of market monitoring of managers is higher than it was before the death of the cross-shareholding regime.

What is much clearer is that the governance of Japanese takeovers has shifted away from the informal arena of stable shareholding to the formal institutional arena of courts. It is in this formal venue that the future of the Japanese market for corporate control will be determined. This is a significant institutional change. How it happened is the subject of this chapter.

[1] Schaede (2008), Ahmadjian (2007).
[2] Gilson (2004), Witt (2006).
[3] Vogel (2006), Jackson and Miyajima (2007).

The overwhelming problem for Japanese business in the 1990s was how to move beyond the economic stagnation of the decade after 1993, retrospectively called the "lost decade" by most Japanese. The economic crisis drove many Japanese large companies to change their competitive strategies at the end of the 1990s as they began to focus on their core business and to spin-off unrelated subsidiaries.[4] Like their counterparts in France, managers of large companies in Japan were able to restructure aggressively because of the weakness of labor representation at the company level. Japanese firm-based employee organizations lack the legally mandated rights enjoyed by Dutch and German works councils. As Gregory Jackson has argued, this weaker institutionalization of labor at the level of the firm has made it much easier for Japanese firms to introduce measures aimed at increasing shareholder value, even when labor organizations might be opposed to such measures.[5] The competitive strategies chosen by Japanese business led many to seek out foreign institutional investors, and those foreign investors in turn pushed managers further in the direction of maximizing shareholder value.[6] Firms with higher levels of foreign investment during this period were more likely to downsize employment or to reorganize by selling off parts of the company.[7] The political consequence of this firm-level change was the focus by the peak association of managers, the Keidanren, on reforming corporate law so as to facilitate this process of restructuring.[8]

The destruction of stable shareholding in Japan took place against this same backdrop of an economy in crisis. As share prices collapsed in the late 1990s, banks with large cross-shareholdings had to sell those shares to meet the capital requirements of the Bank for International Settlements (known as the Basel II requirements). Many banks were perceived by nonfinancial corporations to be increasingly risky investments. As one company involved in cross-shareholding with another sold its shares, the other company was likely to respond in kind.[9] The unraveling of cross-shareholding was not driven primarily by views about takeover protection, but by the short-term challenges posed by the economic crisis. It was not an intentional decision, on the part of either companies or government officials.[10] The death of Japanese patient capital was really a case of manslaughter, not of murder.

4 Schaede (2008).
5 Jackson (2003, 2007).
6 Tiberghien (2007).
7 Ahmadjian and Robins (2005), Ahmadjian (2007).
8 Vogel (2006), Gilson and Milhaupt (2004). The Keidanren (the Japan Business Federation) has historically been the political defender of large corporations in Japan (Hamada 2010). In 2002, the Keidanren merged with the Nikkeiren, a formerly separate organization of employers' associations responsible for social and employment-related issues (Vogel 2006: 56–57). Large firms are well-represented at the Keidanren. Its first postmerger chairman was Hiroshi Okuda, president of Toyota Motor Corporation. Fujio Mitarai, chairman of Canon, succeeded Okuda in 2005.
9 Miyajima and Kuroki (2007).
10 The Basel II capital adequacy requirements were the product of an international regulatory action, but they were not aimed at eliminating cross-shareholding in Japan or elsewhere.

The breakdown of shareholding networks as takeover protection was accompanied by the emergence of isolated hostile takeover bids in Japan after 1999. However, these bids were all for small companies. No large Japanese company was the subject of a hostile attack prior to 2004. For managers acting through the Keidanren, there was no apparent cost to donning the mantle of economic reformers in terms of autonomy lost to other market players or threats to internal work organization.

That changed with the onset of two events in 2004 and 2005: the UFJ/Sumitomo battle and the attempted hostile takeover of Nippon Broadcasting (NBS) and the broadcasting giant, Fuji TV. The prospect of a hanging concentrates the mind, and these two episodes brought home to managers of Japanese large companies that the changes in the market for corporate control were not only of concern to small company managers. Japanese large companies are generally more reliant on firm-level cooperation with their workforce than are the smaller companies involved in earlier takeover bids.[11] As a result, the majority of large companies in Japan opposed the introduction of rules that could make these companies themselves the object of hostile takeover bids.

From a focus on the flexibility of law as a tool for reorganizing companies in the early part of the decade, the Keidanren moved toward a much more aggressive use of the political system to regulate hostile takeovers.[12] Having abandoned long-term shareholding with other companies, Japanese managers were fortunate in that some bureaucrats had already begun thinking at this time about what sort of measures of takeover protection might be helpful to Japanese business. The most important set of guidelines governing hostile takeovers would not come in the form of laws or regulations, but from an informal advisory group convened by the Ministry of the Economy, Trade, and Industry (METI) and the Ministry of Justice (MoJ). This Corporate Value Study Group (CVSG) developed a new set of institutional rules for "fair and reasonable" takeovers and the defenses firm management could deploy against them.[13] The group was an initiative of the bureaucracy, not of organized managers. Yet the position of organized managers in its informal deliberations allowed them to have a significant influence on the final rules the group produced, even though it was an issue about which most large company managers had been unconcerned at the beginning of 2004.

In 2005, the attempt by a maverick internet company, Livedoor, to acquire a corporate giant generated widespread public interest in the subject of hostile takeovers in Japan. After this event, corporate control became an issue of high political salience in Japan. Under these conditions, the Keidanren would encounter difficulties achieving its political objectives in trying to derail a new

[11] I am indebted to an anonymous reviewer for emphasizing this point.

[12] Vogel (2006).

[13] Thanks to Curtis Milhaupt for suggesting this phrasing of the new METI standard for acceptable hostile takeovers.

style of merger known as the triangular merger. Japanese business is still an important interest group under conditions of high salience, but it was unable to dominate other actors in the governance space when the public and political parties were paying close attention to the policy domain. The triangular merger episode is the only one in the book where we can say that organized managers failed in their objectives for a regime of corporate control, and it took place in a time when corporate control had achieved a high level of political salience. I argue that the tools of managers, which had allowed them to be so influential in earlier episodes of reform, worked less well under the conditions of sustained political salience.

The Political Narrative of Japanese Corporate Control, 1997–2007

Between 1997 and 2004, the liberalization of Japanese corporate governance was overdetermined. Every actor that we would expect to matter in affecting the outcome of deregulatory battles favored liberalization. Managerial organizations all pushed for liberalizing regulations, as did foreign and domestic institutional shareholders and reformers within the ruling party. The general pattern of reform, as described by Steven Vogel, was one in which business and government jointly pushed for regulatory changes that gave Japanese companies more options.[14] The rise of shareholdings by foreign investors, and the more aggressive pursuit of shareholder value by domestic institutional investors was plainly in evidence in Japan in the early part of the century.[15] At the same time, entrepreneurial actors in the ruling LDP and the bureaucracy teamed up to support an aggressive program of reform of corporate law.[16] This was a project of reform that the Keidanren actively endorsed and partially initiated.[17] However, studying the consensual aspects of corporate law reform can tell us little about the relative power of these actors in the political sphere.

This chapter examines how these actors fared in three important and non-consensual episodes affecting the Japanese regime of corporate control. These actors are the most relevant ones to investigate because they represent the most plausible operationalization of the different theoretical approaches compared in this book. In coalitional theory, the rise of powerful institutional investors, both foreign and domestic, can swing the balance of power in institutional reforms that move away from stakeholder protection toward shareholder rights.[18] Theories of partisanship expect change to be pushed by political parties. The theory of quiet politics predicts that managerial organizations will prevail under conditions of low political salience because of their capacity for lobbying and their

[14] Vogel (2006).
[15] Ahmadjian (2007), Schaede (2008).
[16] Tiberghien (2007).
[17] Shishido (2007), Vogel (2006).
[18] Gourevitch and Shinn (2005). The other potential coalitional actor – unions – played almost no role in discussions of Japanese corporate law reform (Vogel 2006: 94).

ability to wield influence through informal groups where they are included because of their expertise.

The first episode of interest conflict was not directly over an issue of corporate control. It was, though, regarded by observers as the key conflict over whether the Japanese system of corporate governance would converge on the American system.[19] The Ministry of Justice (MoJ) and the Ministry of the Economy, Trade, and Industry (METI) in 2001 both favored a legal reform that would require all Japanese large companies to have at least one director appointed from outside the company.[20] This was known as "U.S.-style" board reform. The mandatory appointment of independent board members is characteristic demand of stakeholder activists who argue that such directors provide a better check on management than those with direct ties to the company. The Keidanren, lobbying through parliament, was able to convince legislators instead to adopt a rival commercial law proposal that made the choice of board structure optional. That is, firms could choose to have independent directors or they could remain instead with the traditional Japanese system of statutory auditors. The Diet (the Japanese Parliament) adopted this rival proposal in 2002. The vast majority of listed companies did not opt for independent boards. Most of the companies that did opt for this American-style corporate structure were perceived as having extremely internationally oriented senior managers, as in the case of Sony.[21] In the most significant battle that divided the reforming coalition prior to 2005, the Keidanren view prevailed.

The most important change to the rules governing Japanese takeovers did not take place through the adoption of a new law, but through the promulgation of an informal code in 2005. METI and the MoJ had jointly convened the Corporate Value Study Group as a forum to develop guidelines about the legality of takeover defenses in Japan while the issue was not on the public radar. A major question debated by this group was whether to permit the use of poison pill takeover defenses, as allowed under Delaware law in the United States, or instead to adopt the strict board neutrality requirement in the City of London of the United Kingdom, which was the basis for the EU takeover directive.[22] In the choice between the UK- and U.S.-style takeover guidelines, the investor coalition and neoliberal reformers should both favor the UK-style City Code, which is less protective of managers and more concerned with the problem of shareholder value. The Delaware model, by contrast, provides more protection to management by allowing barriers to hostile takeovers.

The final episode of the battle over corporate control in Japan took place in the formal arena under conditions of high salience. These are conditions

19 Gilson and Milhaupt (2004).
20 Tiberghien (2007).
21 Gilson and Milhaupt (2004).
22 Milhaupt (2005); interview with Hideki Kanda, Chair, Corporate Value Study Group, and Professor of Law at the University of Tokyo, June 5, 2007.

TABLE 5.1. *Summary of Theoretical Predictions in Japanese Corporate Politics, 1997–2007*

Predictions →	**Quiet Politics [Manager-Led]**	**Coalitional Theory [Investor-Led]**	**Partisanship [Party-Led]**	**Outcome**
Law on Board Structure (2001–2002): Low salience	Independent board optional	Independent board mandatory	Independent board mandatory	Independent board optional
Corporate Value Study Group (2004–5): Low salience at outset	Poison pills allowed	Poison pills banned	Poison pills banned	Poison pills allowed
Triangular Merger Law (2005–2006): High salience	Liberal bill implemented	Liberal bill implemented	Liberal bill implemented	Liberal bill implemented

under which we expect the positioning of political parties and public opinion to be the decisive variables, as predicted by coalitional theorists. This episode involved a legal amendment enabling the use of triangular mergers. Triangular mergers allow potential acquirers to establish a subsidiary company in Japan, and then use stock of the parent company as consideration in a merger with another company in Japan. One goal of the reform was to promote foreign direct investment in Japan by making it easier for foreign firms to acquire domestic ones. This device was applicable only for friendly mergers – where both boards of directors approved – but it became embroiled in the general debate about hostile takeovers in light of concerns of Japanese companies from 2004 that they might face a threat from potential acquiring firms located elsewhere. And the battle directly opposed the organization of large business, the Keidanren, and interest groups and partisan actors favoring neoliberal reforms. Under these circumstances, the liberal coalition prevailed, although the Keidanren managed to extract an amendment delaying the implementation of the measure. Organized business is a strong actor even under high salience, but the decisive conflicts are likely to happen within political parties once an issue attains durable salience, which militates against the business dominance we have observed elsewhere in the domain of corporate control.

Table 5.1 presents the theoretical expectations of the different approaches in the current literature on the politics of corporate control, as well as the actual outcome of these episodes. The quiet politics approach anticipates that when salience is low and preferences over laws or informal rules diverge within the reformist coalition, the preferences of organized managers are likely to prevail. The coalitional approach focuses on the rising role of foreign investors in Japanese companies and the concomitant political power these groups exercise in the Japanese polity.[23] If coalitional politics were the driver of change in the market for corporate control in Japan, we would expect foreign investors to team with liberal managers and/or liberal politicians to impose the most shareholder-friendly outcomes on recalcitrant managers. In Japan, the battle over neoliberal reforms never involved the parties of the left, suggesting that Cioffi and Höpner's stress on the left as the ineluctable force for reform in corporate governance is falsified for Japan.[24] However, one can expand the partisan theoretical approach to include all work focused on parties and their leadership as the agents of change. Such an approach stresses instead the causally important role of the maverick prime minister, Junichiro Koizumi, and the reformers whom he promoted in the ruling Liberal Democratic Party (LDP), such as Yasuhisa Shiozaki.[25] This version of the partisan approach is the one assessed in the following discussion.

The remainder of this chapter shows how and why managers were able to achieve their preferred outcome over the objections of politically powerful opponents. Hostile takeovers and the market for corporate control were low salience issues from 1997–2004, which enabled the Keidanren to achieve many of its objectives during this period through its direct lobbying in parliament or through cooperation with the bureaucracy. As I show in the next two sections, the events that galvanized the Keidanren to adopt more conservative positions on reform, at the end of 2004 and beginning of 2005, also brought the issue of hostile takeovers to general attention and higher salience. This increased the leverage of reformers in the LDP because the initial wave of coverage of the Livedoor takeover bid painted Livedoor in a positive light.[26] Yet the issue was not debated in parliament, but in an informal working group whose members had been determined before the rise in political salience of hostile takeovers. In this group, managerial interests were well represented and managerial opponents were not. Thus, the informality of the Corporate Value Study Group guidelines preserved managerial influence even in a high salience atmosphere.[27] The final section explores the lobbying efforts of the various actors in the implementation of the triangular merger law.

Japanese Managerial Preferences

Between 1997 and 2004, the overriding concern of managerial organizations and of political reformers in the LDP was to restructure companies in order to

[23] Schaede (2008), Ahmadjian (2007).
[24] Cioffi and Höpner (2007).
[25] Tiberghien (2007).
[26] Whittaker and Hayakawa (2007).
[27] Livedoor's positive image proved short-lived, as its charismatic CEO, Takafumi Horie, was arrested on charges of financial malfeasance in early 2006.

end Japan's economic crisis. The sharp fall in long-term shareholding, which had previously provided hostile takeover protection for many Japanese companies, did not kindle any significant concern among managers of large firms. Indeed, these managers were at the forefront of pushing for legislation that would provide more tools to enable corporate reorganization.[28] Three-quarters of the 472 largest companies in Japan reported undertaking some form of corporate reorganization between 2000 and 2006.[29] These measures of restructuring were facilitated by a host of legal changes made at the end of the 1990s with active managerial support.

During this period of economic crisis, the political organizations of Japanese managers were not proponents of a more active market for corporate control, but neither were they opposed to it. The fall in stable shareholdings that came about during this period went hand-in-hand with the beginnings of activity in the previously quiescent hostile takeover market. The companies involved were small. There was no political concern about this trend among managers of large firms, nor was this phenomenon of interest to the wider Japanese public. These takeovers were seen as signs of the restructuring that the Keidanren had been advocating. Japanese managers of large firms only began to be concerned in the summer of 2004, when the UFJ merger deal made it clear that the rules of the game had also changed for large companies. The attempt by Livedoor to acquire the media giant Fuji TV catalyzed this rising managerial concern and also caught the interest of the public.

The Beginnings of an Active Market for Corporate Control

The first successful hostile takeover in Japan occurred in 1999 when the British firm Cable & Wireless took over International Digital Communications (IDC), a small telecommunications company. Two takeover attempts took place the following year, including the first ever hostile takeover bid launched by one Japanese company against another. M&A Consulting (MAC), a company led by former METI high-flyer Yoshiaki Murakami, launched a bid against Shoei after failing to convince the company's management to change its strategy. The MAC bid was seen by the press and some scholars as the end of the norm against hostile takeovers in Japan.[30] Both Murakami and the firm that financed his bid, the financial services group Orix, were considered outsiders by the Japanese managerial establishment.[31] The extent to which such outsiders could change mainstream managerial norms about takeovers is questionable.[32] In the two years after the deal, the only unsolicited bids in Japan were launched by Japan Steel Partners (JSP), an American fund. MAC and JSP were involved in a variety

[28] Vogel (2006).
[29] Schaede (2008: 11).
[30] Milhaupt (2001).
[31] Commenting on Orix's backing of the MAC bid for Shoei, a Japanese banker interviewed by Milhaupt (2001: 2114) said, "That's the type of thing Orix would do. Big Japanese banks wouldn't dare – they worry too much about what others would think."
[32] Culpepper (2005).

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TABLE 5.2. *Unsolicited Deals in Japan, 2000–2004*

Target Firm	Hostile Acquirer	Month/ Year	Transaction Value ($ million, year 2000)	Takeover Successful?
SS Pharmaceutical	Boehringer Ingelheim	1/2000	207.1	Yes
Shoei Co.	M&A Consulting	1/2000	133.4	No
Yushiro Chemical	Steel Partners Japan	12/2003	135.0	No
Sotoh	Steel Partners Japan	12/2003	192.9	No
Kintetsu Buffaloes	Livedoor Co.	6/2004	16.3	No
Miyairi Valve	Banners Co.	6/2004	71.3	No
UFJ Holdings	Sumitomo	7/2004	29,674.6	No

Source: RECOF; information on corporate valuation from T1B database, except for Kintetsu (from public sources) and Miyairi (from McKinsey Tokyo).

of shareholder activism cases, in the years between 2001 and 2004, but the perception of much of corporate Japan was that these companies were acting as "greenmailers," using takeover bids against smaller companies to convince management to raise dividends paid to shareholders. When asked about the impact of the Shoei case on general managerial perceptions of takeovers, one senior M&A lawyer I interviewed observed that "Shoei is maybe not a good case. It was conducted by Murakami, and Murakami and Steel Partners were considered greenmailers."[33] As Table 5.2 shows, these two companies were the only ones active in the takeover market prior to 2004, and their targets were exclusively small companies, as indicated by the column in Table 5.2 on transaction value.

Politically, there was no pressure from leading managers in the Keidanren to intervene in the area of hostile takeover regulation at this time because they favored corporate restructuring and because Murakami's bid was not perceived as a threat. A senior Keidanren official whom I interviewed summarized the organization's view toward the Shoei takeover in the following terms:

> At first we were not concerned, because [Murakami] was an ex-MITI bureaucrat running a fund. This was quite an anomalous actor.... Our business attitude was, wait and see.... From the viewpoint of the Japanese business

[33] Interview, mergers and acquisitions lawyer, Mori Hamada & Matsumoto Law Firm, April 25, 2007. Curtis Milhaupt argues that MAC's takeover attempt was primarily an attempt to change the norm against hostile takeovers. This interpretation of Murakami's intent is consistent with what I was told by a former high-level bureaucrat from METI: "Murakami is a former METI guy; I know him well. He came to me when he left METI and said, 'METI changed the rules but unless management feels that they have to change, these new rules won't mean anything. So I'd like to start a fund to push managers to be active in using the assets given them by shareholders.' He started a small fund – did Shoei and Tokyo Style [another small company for against whose management Murakami led a proxy fight]. These [companies] were small, but [Murakami's] mouth was big." (Interview, former METI official, April 20, 2007).

> community, Shoei is a miniscule company. Its takeover did not attract much attention from big companies. . . . In 2001 and 2002, the top agenda item was how to deal with non-performing loans and restructuring. We thought funds, like Murakami and others, were going to play a role in the buying and selling of these assets. . . . If Murakami had gone after key companies in the Keidanren, this might have caused concern.[34]

Between 1997 and 2003, the legislative attention of the Keidanren was fixed squarely on the problem of reforming corporate law to enable them to reorganize, not on the issue of corporate control. As summarized by legal scholar Zenichi Shishido, the reform of corporate law,

> such as deregulation of share purchases, stock options, and reorganization schemes, were demand-pull reforms. In other words, business sectors demanded these deregulations of what had been prohibited by Japanese corporate law, which has many more mandatory restrictions compared with American corporate law. Japanese management wanted to do what American management could do.[35]

The consistent line of Japanese business was that liberalization should provide more options for business, and the Keidanren's political priorities clearly reflected this line between 1997 and 2003.[36]

What political resources did the Keidanren use to pursue its political preferences for liberalization? Structurally, the business organization has a seat on the Legislative Council of the Ministry of Justice (MoJ), which is the central administrative authority for reforming corporate law. This allows it to review and influence proposed legal reforms. The organization also maintains representation in the deliberative councils (*shingikai*) set up by major ministries with interests in corporate and economic reform, including METI and the FSA.[37] The Keidanren maintains close ties to legislators in the ruling LDP, as well as in other political parties. A Keidanren lobbyist I interviewed in 2008 told me that the best tactics for lobbying depend on the political context.

> Right now, politicians are losing power – populism is on the rise, and the mass media and the bureaucracy are gaining power. When Koizumi was in office [2001–2006], politicians had a lot of power, and our lobbying was focused on the LDP, because they had the chance to make the difference.[38]

In the reform of corporate law, the Keidanren's direct ties with legislators would prove instrumental in getting around bureaucratic opposition to reforms of corporate governance.

[34] Interview, senior official of economic policy directorate, Keidanren, April 18, 2007.
[35] Shishido (2007: 322).
[36] Vogel (2006).
[37] Yoshimatsu (2000), Estevez-Abe (2008). The FSA is the Financial Services Agency, which is responsible for securities law.
[38] Interview, lobbyist for Keidanren, April 10, 2008.

Legal scholars describe the changes in Japanese corporate law between 1997 and 2003 as a sea change representing the "most sweeping and fast-paced changes to corporate law" in a century.[39] The vast majority of these changes were supported aggressively by the Keidanren.[40] The MoJ is often considered conservative in the area of reform and in the late 1990s the Keidanren and reformers within the LDP joined forces to bypass the MoJ. In passing a law that legalized stock options and simplified merger procedures, the employers' organization used a parliamentary maneuver, a member's bill, to circumvent the MoJ and some conservative LDP-members.[41] The procedural device of the member's bill, heretofore rarely used in the domain of corporate law, was employed five times between 1997 and 2003 by members of this reforming coalition who wanted to go around conservative opposition.[42] By all accounts, lobbyists of the Keidanren and the reformist wing of the LDP worked together as close allies in this reform process.[43]

Because the LDP was divided between a reformist and a traditionalist faction, as were the bureaucracies involved in reform, the Keidanren occupied a pivotal position in the corporate reform process. It was able to rely on a reformer in the LDP to present member's bills when it wanted to overcome traditionalist opposition, as in the stock options case. Yet many reformist politicians also looked to the Keidanren in making judgments about the desirability of new reforms. The battle in 2001–2002 was the first significant division within the reformist alliance. According to Yves Tiberghien, "Keidanren was suspicious of METI because of its international openness agenda, an agenda pursued since the 1960s and because of the close personal links between METI and foreign investors (or the U.S. Chamber of Commerce)."[44] When the alliance between METI and foreign investors attempted to impose a METI plan on recalcitrant managers, the Keidanren convinced Seiichi Ota, chair of the LDP subcommittee on commercial law and author of the original (proreform, pro-Keidanren) member's bill in 1997, to propose another member's bill making the choice of independent directors optional.[45] The government ultimately adopted this formulation in its compromise legislation in 2002. In one of the few clear moments of opposition between the different members of the

[39] Milhaupt (2003: 5).
[40] Tiberghien (2007), Shishido (2007).
[41] Vogel (2006: 92–93).
[42] Tiberghien (2007: 148–154). The head of the Economic Law Bureau of the Keidanren during this epoch noted that the Keidanren also established a think tank in 1997. The 21st Century Public Policy Institute was established to provide a source of expertise for legislators who wanted to propose member's bills. "Some politicians started to indicate interests in making laws by their way of thinking, such as [Yasuhisa Shiozaki, a prominent reformer]; we call them the new generation. So, I think this institute, in my personal opinion, would have been able to help the new generation to make laws by Diet members, not bureaucrats" (interview, April 15, 2008).
[43] Vogel (2006), Tiberghien (2007), Shishido (2007).
[44] Tiberghien (2007: 153).
[45] Vogel (2006: 92); Gilson and Milhaupt (2004).

reformist coalition, the ability of the Keidanren to rely on key supporters in parliament allowed it to get the legislation it preferred.

The Keidanren Turns Against Takeovers

Organized managers in Japan only turned against the liberalizing agenda in corporate law in 2004. From the perspective of the Keidanren, though, this was not a large change. Its consistent line in the rapid reforms between 1997 and 2003 had been to use corporate law to create more options for managers to reorganize their firms.[46] The existence of funds like MAC, for example, were perceived as helpful resources for reorganization; threats to small firms, yes, but not to the managers of large firms. The battle between the giant banks Sumitomo and Mitsubishi for control of a third large bank, UFJ Holdings, shifted the terms of the conversation about hostile takeovers in Japan. As Table 5.2 makes clear, Sumitomo's hostile bid for UFJ was an order of magnitude larger than any of the bids that had taken place previously. It was, moreover, a battle between two large banks that sat at the center of Japanese business networks. Whereas the previous bids had come either from foreign firms or domestic outsiders (like Murakami), the bid from Sumitomo came from the heart of the Japanese business network.[47] As such, it was more likely to capture the attention of large business elites than were earlier bids for small companies from corporate outsiders.[48]

The UFJ case received so much attention not only because of the size and identity of the participants in the takeover battle, but also because of the tactics used, which broke with accepted business practice in Japan.[49] In May 2004, UFJ agreed to sell its trust bank to Sumitomo. The contract included a provision preventing either bank from negotiating with third parties in a manner that could obstruct the deal. Yet in July 2004, UFJ agreed to merge with the Mitsubishi Group (MTFG) in a deal that would result in the largest bank in the world, based on assets, at that time. Sumitomo sued to invalidate the transaction, which was initially stopped by the court, but that ruling was then reversed in a high court decision in August, after which the boards of UFJ and MTFG approved the merger. Sumitomo then attempted to pressure the UFJ board by publicly launching its own hostile offer for UFJ Holdings (a tactic called a "bear hug" in mergers and acquisitions).[50] Following the upholding of the UFJ/MTFG deal by the supreme court, UFJ issued preferred shares to MTFG to help protect it from Sumitomo's ultimately unsuccessful bid (ibid). In legal terms, the case was noteworthy both for the fact that UFJ reneged on its original deal with Sumitomo, and for the aggressive response pursued by Sumitomo through the courts.[51] Even the American financial press claimed that the outcome of the

[46] Vogel (2006).
[47] Scott Jones, a practicing M&A lawyer in Tokyo, described Sumitomo as the first of the "domestic old-boy raiders" (Jones 2007).
[48] Cf. Culpepper (2005).
[49] This paragraph relies on the account of the UFJ/Sumitomo fight presented in Milhaupt (2005).
[50] Milhaupt (2005).
[51] Milhaupt (2005).

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UFJ case "represents a paradigm change on the legal side. It shows a more legally aware business mind-set in commercial dealings. The days of unspoken understandings underpinned by personal relationships are fading away."[52]

The UFJ deal itself was not of direct concern to the Keidanren, which took no position on it. The legal questions it raised, though, were of central import to the managerial organization. On November 16, 2004, the Keidanren issued a policy paper in which it announced a new concern about hostile takeovers. The policy statement began by noting that the organization had promoted several changes in company law over the past years, and that these changes had led to a desirable increase in foreign direct investment. It then sounded a new note of caution:

> However, over the last few years we have seen the unwinding of cross-shareholding and a decline in the aggregate value of listed stocks caused by a slumping stock market. These negative factors, together with the lack of reasonable defense mechanisms, have led to growing fears of takeovers that would harm corporate value.[53]

This was the organization's first public expression of concern about the threat of hostile takeovers in Japan since the reform process of 1997 had begun. The document then went on to suggest that triangular mergers were one tool that posed a threat to the Japanese model of stakeholder capitalism. This was a reversal of position on the desirability of triangular mergers, as a Keidanren lobbyist explained to me: "On the triangular merger law, for example, we changed our mind. Keidanren initially proposed it in 2002. We proposed it as a way to get more foreign investment, which we thought would be good for Japan. And then later we decided it was dangerous."[54] The change of position was striking enough to warrant commentary in an *Asahi Shimbun* editorial on December 9: "This sort of foreign capital phobia has even spilled over to the pro-deregulation Keidanren camp.... Up until now they had been saying exactly the opposite [on the desirability of triangular mergers]." The position paper of November 16 foreshadowed the two important episodes of reform in the market for corporate control: the discussion of hostile takeover defenses and the implementation of the triangular merger law.

Political Salience and Livedoor

Until 2004, hostile takeovers were not an issue of great importance for the Keidanren. And if a *managerial* organization cares little about hostile takeovers, it is likely that the issue will have low political salience with the wider public. In fact, as we shall see in this section, the Japanese public paid very little

[52] Fackler and Sender (2004).

[53] Keidanren (2004), "Reasonable Defense Measures against Takeovers Detrimental to Corporate Value are Needed" (available at http://www.keidanren.or.jp/english/policy/2004/085.html; downloaded 1/12/09).

[54] Interview, lobbyist for Keidanren, April 10, 2008.

attention to the issue of hostile takeovers between 1997 and 2004. That situation would change dramatically in January 2005, when the internet firm Livedoor launched a takeover bid for Nippon Broadcasting (NBS), the parent company of Fuji TV.[55] The CEO of Livedoor was Takafumi Horie, a brash young entrepreneur who was rarely seen in a tie but often seen in a sports car. He styled himself the enemy of old corporate Japan. In his initial bid for NBS, public sentiment largely viewed Horie in a positive light.[56] Within the Keidanren and its LDP allies, however, the reception to Horie's bid was one of alarm. As a manager at a large financial holding group told me, "Fuji TV is huge, and so the big companies thought, 'oh, it could happen to us too.'"[57] The Livedoor takeover attempt galvanized managerial concern about the risk of takeovers even as it brought the issue to broad public attention.

To assess the political salience of hostile takeovers in Japan, I relied on a review of press coverage of five major Japanese newspapers.[58] These five national papers cover most of the most political spectrum in Japan. With the help of two Japanese-speaking research assistants, I used the Nikkei Telecom21 database to compare the salience of hostile takeover politics with three other technical domains of economic policy: bargaining rules (over wages and working conditions); the pension system; and youth vocational training.[59] Tracking

[55] Fuji TV was the fiftieth largest company in Japan by market capitalization in the year 2000.

[56] Whittaker and Hayakawa (2007); Nakamoto (2005). One survey by an Asahi news program found that even older people – sixty percent of those in their 50s and 60s – supported Horie (Nakamoto 2005). One business reporter for the *Yomiuri Shimbun* whom I interviewed disagreed with the assertion that press coverage of Horie and Livedoor was sympathetic: "NBS is a broadcast company. Every major newspaper has its own broadcast network. There was a worry that if Horie succeeded, we [journalists] could be vulnerable to attack. We tried to protect NBS. We were not neutral in [our] coverage." (Interview with staff writer, *Yomiuri Shimbun*, May 2, 2008).

[57] Interview, senior executive at Millea Holdings, April 15, 2007.

[58] The newspapers included were the *Yomiuri Shimbun*, the *Asahi Shimbun*, the *Mainichi Shimbun*, the *Nihon Keizai Shimbun* (*Nikkei*), and the *Sankei Shimbun*. Of the seven newspapers with the highest circulation in the world six are Japanese. As of 2007, the *Yomiuri Shimbun* had the highest circulation in the world, with ten million subscribers; the *Asahi Shimbun* was second, with eight million; the *Mainichi Shimbun* had almost four million subscribers; the *Nihon Keizai Shimbu*n, the business newspaper of record, had three million; and the *Sankei Shimbun* had two million (see http://adv.yomiuri.co.jp/m-data/english/2008_2010/newspaper1.html and http://www.wan-press.org/article2825.html; downloaded 1/12/09).

[59] These searches were performed by Tomohiro Hamawaka and Nathan Cisneros, for whose assistance I am grateful. To create institutional categories that were as conceptually comparable as possible, the search relied on terms that would capture articles dealing with rules of governance in each issue area. The search terms used were the following (English translation is followed by bracketed Japanese original):

Takeover Protection: "(takeover or merger) and (protection or bid) and (hostile)" [(買収 or 合併) and (防衛 or 買い付け) and (敵対的 or 非友好)].
Vocational Training: "(youth or youth) and workplace training" [(若者 or 少年) and 職業訓練].
Bargaining Rules: "spring wage offensive" [春闘].
Pension System: "pension system" [年金制度].

the newspaper coverage over time in these areas gives a useful estimate of the relative political salience of these different policy issues over time.

Between 1997 and 2004, there were very few articles in the Japanese press on the subject of hostile takeovers. As in Chapters 3 and 4, Figure 5.1 sets the Mendoza line of political salience at the average annual number of articles on the least well-covered high salience issue measured. In Japan, this issue is bargaining rules. The average number of articles per year on bargaining rules in the Japanese press was 985. By contrast, the average number of articles per year on takeover protection was fifty-seven, which means that fewer than *one article per month* in each newspaper made any mention of hostile takeovers.[60] However, Livedoor's attempt to take over Fuji TV brought immediate public attention to the area of hostile takeovers. In 2005, the average number of articles per paper per month was twenty-five, surpassed only by the almost thirty-eight articles per paper per month in the area of the pension system, and well above our Mendoza line based on the coverage of bargaining rules. While that number declined in 2006, the coverage of hostile takeovers stayed above the Mendoza line and only dipped slightly below it in 2007. In contrast to our other cases, takeover protection was a high salience issue in Japan in 2005 and 2006.

In interviews with actors involved in this policy subsystem, as well as in academic accounts of them, one perception was consistently reported: that coverage of hostile takeovers in the Japanese press was tinged with nationalist reactions against the possibility of foreign takeovers. The main lobbying group for European business, the European Business Council Japan (EBC), released a position paper on foreign direct investment in May 2005, in which it observed "The current debate in Japan gives the impression that foreigners are eager to engage in 'hostile' take-overs of Japanese companies.'"[61] With two research assistants, I attempted to gauge the framing of press articles in this domain, as in the research on France and the Netherlands. We were unable to find any consistent set of frames in the Japanese coverage of hostile takeovers, including one that emphasized the threat of foreign takeovers. Compared with the Dutch and the French press, news articles tended to make little use of metaphors and evocative quotations from leading businessmen. This was all the more surprising because a Keidanren lobbyist I interviewed said that the managerial organization had adopted a new press strategy from 2003 on. "We wanted to get our point of view out in the public domain by talking

[60] This compares with an average of more than eighteen articles per paper per month on the subject of wage negotiation and thirty articles on the pension system (coverage of which spiked in 2003 and 2004).

[61] EBC (2005b) (Position Paper on FDI, http://www.ebc-jp.com/news/2005%20EBC%20Position%20Paper%20on%20FDI%202005%20(English)-May.pdf), downloaded 1/13/09. The American Chamber of Commerce in Japan (ACCJ 2005) observed the same tendency: "Groundless and emotional assertions about an impending "foreign threat" unfairly taint the image of foreign direct investment (FDI) within Japan," (http://www.accj.or.jp/doclib/pc/050516toMETI_E.pdf), downloaded 1/13/09.

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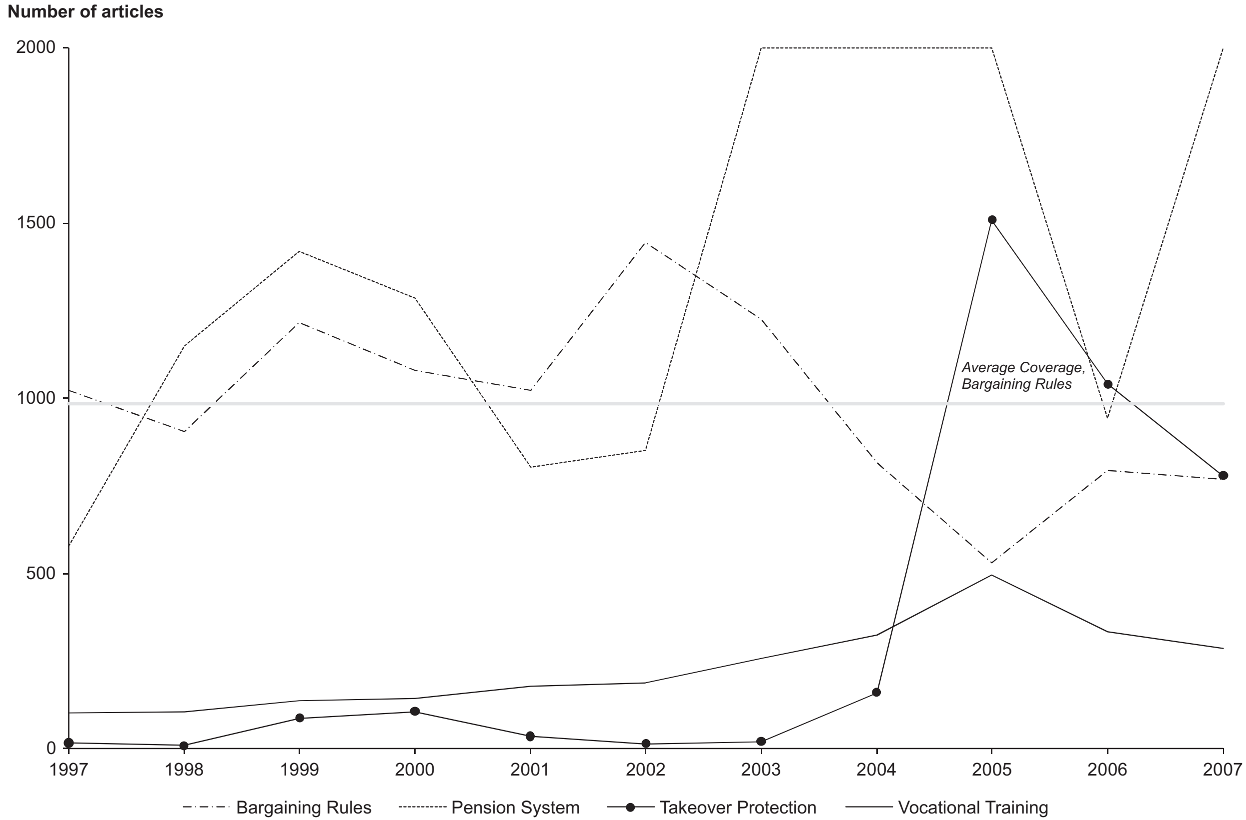

FIGURE 5.1. Political Salience of Issue Areas in Japan, 1997–2007

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to the writers who write about the big issues. [This strategy] was a response to Koizumi, who was a master of using the media."[62] It is possible that the Keidanren succeeded in affecting press coverage in a way that our attempted content analysis was unable to measure, but which actors on the ground, such as the EBC and ACCJ, perceived. Using similar protocols to those we attempted in the European countries, though, it appears that Japanese press coverage of hostile takeovers was more neutral than in the other countries studied.[63]

The theory of quiet politics predicts that a rise in issue salience will blunt the effectiveness of managerial tools of influence, such as direct lobbying of politicians, because those politicians have incentive to respond to voters on the issues voters care about. In 2005, hostile takeovers reached a high level of political salience in Japan as a result of the Livedoor takeover. And indeed, no major reform of hostile takeovers did pass the Diet in 2005. Yet the key reform of Japanese corporate control was never *debated* in parliament. The new rules of corporate control would be elaborated instead by an informal group with no legal standing, a group that had been assembled before the

FIGURE 5.1. Political Salience of Issue Areas in Japan, 1997–2007
Source: Nikkei Telecom21 Database. See footnote 58 for a discussion of search terms.
Note: This graph only shows an annual total for the number of articles appearing on a given subject up to a threshold of 2,000 articles. It therefore understates a spike in the coverage of articles about the pension system between 2003 and 2005 (there were 2,912 articles dealing with the pension system in 2003, 5,571 articles in 2004, and 2,262 articles in 2005). The increased coverage of an already high-salience issue during this period was a product of a major pension reform as well as a scandal related to politicians failing to contribute to their system (Japanese politicians are part of a pension system that requires self-payment as opposed to automatic employer deduction). Even in the peak year of coverage of hostile takeovers in the Japanese press (2005), when the issue was unquestionably of high political salience, there were still more than 750 articles dealing with the pension system than with hostile takeovers. The gray horizontal line shows the average number of articles per year published on the subject of bargaining rules, which is the less covered of the two high-salience issue areas depicted in this figure. This is one rough indicator of a minimal level of media coverage we might classify as being associated with an issue of high political salience.

[62] Interview, lobbyist for Keidanren, April 10, 2008.

[63] The Japanese press corps has been labeled an "information cartel" by one scholar (Freeman 2000). Most government ministries, as well as the Keidanren, have their own press clubs in which reporters from major news organizations have offices in the ministries (or association) with the expenses paid by the ministry (McCargo 1996). Freeman argues that the existence of such clubs leads to a homogenization of news coming out of them, since each reporter gets the same information and all are discouraged from seeking outside scoops. Moreover, she argues that the high circulation of most Japanese newspapers has led editors to avoid alienating readers by taking political positions: "they have largely avoided independent pursuit of scandals involving the elite of Japanese society and have also refrained editorially from taking partisan political stances" (Freeman 2000: 19).

Livedoor affair brought takeovers to public attention. Such informal councils, known as *shingikai*, are often used by bureaucracies in Japan to strengthen their position vis-à-vis the legislature and each other.[64] These groups are composed in a way that favors managerial input and excludes some of their political opponents, including notably institutional investors. Thanks to the initiative of an entrepreneurial civil servant, managers in Japan were able to benefit from this mechanism of quiet politics even in turbulent political conditions.

Informal Influence and the Corporate Value Study Group

The group that developed the key reform of Japanese hostile takeover rules was conceived in the spring of 2004 before the LDP or the Keidanren or the general public paid much attention to hostile takeovers. It was a product of METI's reforming agenda, and particularly of one senior bureaucrat, Satoshi Kusakabe, who had headed the team at METI charged with reforming corporate law. The process through which the corporate value report was developed reveals the structural advantages afforded business in Japanese policy making. The group comprised three types of representatives: managerial interests of non-financial firms; professionals in mergers and acquisitions as well as investment bankers; and legal experts (see Appendix 5.1 for a roster of the group). What is glaring in this list is who was absent. There were no representatives of institutional investors and there were no representatives of labor unions. As an informal advisory group, its composition was not mandated by law, but left up to its organizer. The question debated was not a political one, such as, "What are the competing interests involved in hostile takeover protections?" It was instead, "Given the possibility of hostile takeovers, what rules would be consistent with managerial interests and the practice of corporate law in Japan?" As one investment banker on the group told me,

> it was consensual. Everybody there was interested in poison pills, but no one knew how to introduce them safely (i.e., so that they would stand up in court). And companies were concerned about being taken over. It was like brainstorming: the experts talked alot, and the people from industry tended to do more listening.[65]

Managers were not responsible for the formation of the group. Its very composition, though, reflected the view that rule making was primarily a technical issue to be decided by experts and managers, rather than a distributional one to be decided by a broader set of stakeholders.

Political scientists are often skeptical of arguments that attribute important causal power to decisions made by bureaucrats, unless those arguments have a foundation in the interests of bureaucrats themselves. Some claim bureaucrats

[64] Estevez-Abe (2008).
[65] Interview, member of Corporate Value Study Group, May 16, 2007.

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are agents, controlled by political parties, their principals.[66] Others assume bureaucracies are captured by economic interest groups. There is no evidence that either the LDP or any particular set of economic interests directly drove the decision of Kusakabe to constitute the CVSG. Instead, it appears that METI had a bureaucratic rationale for forming the group, and that the continued low salience of the area gave the organization the possibility of taking a lead role in rule making.

Whereas MoJ is responsible for any change to corporate law, and the FSA is responsible for securities regulation and takeover bids, METI has no legally mandated responsibility for a body of law. Its bureaucratic power derives largely from its convening power. By staking a claim to a role in the discussion of hostile takeovers, before the issue had been discussed in parliament or by other agencies, "METI deftly ensured that it would be at the center of future developments in this important area of economic policy."[67] A senior bureaucrat at the FSA, which is widely considered to have a competitive relationship with METI, summarized Kusakabe's motivations in these terms:

> While our financial councils are written in law, [Kusakabe] created an informal group of key players. His leadership and strategy was central to its function. METI has good officials, but they do not control the law. So they are always looking for the next subject.[68]

When I asked Kusakabe himself why METI led the formation of the group, rather than MoJ, he answered,

> MoJ had other things to do. And METI has close relations with the front lines of economic industry. So it's easier for us to take up these activities.... It is customary in reforms in Japan for METI to make the preparation first; then other agencies will follow the lead of METI.[69]

With MoJ active in finishing its reform of corporate law, and both the Keidanren and the LDP unconcerned about hostile takeovers in early 2004, the political space was open for METI to play an agenda-setting role.[70]

The self-described mission of the Corporate Value Study Group was "to change the business community from one without rules [about hostile takeover

[66] Ramseyer and Rosenbluth (1993).

[67] Milhaupt and Pistor (2008: 104).

[68] Interview, official at FSA, April 17, 2007.

[69] Interview with Satoshi Kusakabe, METI (convenor of the Corporate Value Study Group), June 26, 2007.

[70] Cf. Tiberghien (2007). In recruiting participants for the panel from industry in early 2004, Kusakabe reported having difficulty finding managerial representatives who were interested. The two exceptions he reported were from Toyota, whose management had been interested in the issue of hostile takeovers since a celebrated but failed hostile bid for one of its suppliers in 1989; and Yamanouchi, a pharmaceuticals company which was in the process of merging with another company to form Astellas (interview with Satoshi Kusakabe, METI convenor of the Corporate Value Study Group, June 26, 2007).

protections] to one governed by fair rules applicable to all."[71] In September 2004, just after the Sumitomo/UFJ battle, the group oriented its second session around defining the perceptions of Japanese business. A METI survey of listed firms found that eighty-five percent of the companies surveyed "felt threatened" by hostile takeovers. Yet a majority of respondents said they would not adopt measures to prevent such a takeover: one-third because they were uncertain if the measures were legal, and one-third because they worried about the reaction of the markets to the adoption of takeover defenses.[72] The goal of the group was therefore to determine if, and under what conditions, takeover protections could be legal in Japan.

The name of the group, chosen by Kusakabe and the chair of the committee, the eminent legal scholar Hideki Kanda, was itself illustrative of how that question would be answered. According to Kusakabe, "I discussed [the name of the group] many times with Professor Kanda. We considered 'anti-takeover defense measure study group,' but this was too straightforward. It ultimately came from Kanda's philosophy: whether a takeover is good or not depends on its effect on corporate value."[73] Kanda added in his comments to me that,

> We thought about 'shareholder value group,' but we thought [shareholder value] was only part of the question.... We wanted to allow takeovers that would improve 'corporate value' and stop those that did not – corporate value for the shareholder, but also for society at large. [Some people on the group were] arguing strongly in favor of protecting shareholder value. But the name of the group meant some of this issue had already been decided.

As stated in the report itself, the group's goal was to produce "fair" rules for takeover defense, which satisfied the considerations of both corporate value and those of global standards, that is, "on a par with those adopted in the United States and European countries."[74]

The group reviewed the legal arrangements surrounding takeover protection in other countries, including the United States and the European Union (particularly the United Kingdom, Germany, and France). A central problem for the group was whether or not takeover defenses would be consistent with the principle of shareholder equality enshrined in Japanese company law.[75] The report ultimately determined they were, and then made a series of recommendations enumerating the features of rights plans (poison pills) that could be allowed under Japanese law. This choice essentially adopted the Delaware

[71] METI (2005: 8).

[72] METI (2005: 21–23, 108). METI polled forty large institutional investors (twenty from the United States and twenty from the United Kingdom) about their potential reactions to adopting takeover protections as a way to find out the "market" response to takeover protections.

[73] Interview with Satoshi Kusakabe, METI (convenor of the Corporate Value Study Group), June 26, 2007.

[74] METI (2005: 25). The report also enunciated principles of nondiscrimination between foreign and domestic companies and increasing options for shareholders and investors.

[75] METI (2005: 79).

standard from the United States, rejecting the strict neutrality of boards required by UK law (and incorporated into the EU takeover directive, as discussed in Chapter 3). This is not because of the obvious superiority of Delaware law nor for its better fit with Japanese legal traditions. As Milhaupt observes,

> the City Code [arguably] represents a more attractive candidate for transplant into Japan than Delaware takeover law. Its relatively straightforward rules are much simpler to replicate and easier to enforce than a complex body of foreign judicial doctrine. And the quasi-administrative role of the Takeover Panel is more consistent with traditional Japanese approaches to economic regulation than is Delaware's court-centric approach.[76]

The attraction of the Delaware standard was not that it was the most easily reconcilable with the Japanese principle of shareholder equality nor that it represents the unique global standard. The UK City Code is plausibly more attractive on both these dimensions.

Instead, the choice of the Delaware standard appears to have been a product of both familiarity with the lawyers on the panel and an appeal to the interests of METI, lawyers, and managers – the three interests represented in the study group. One member of the Study Group noted the bureaucratic incentive for METI to favor the Delaware standard. "The UK style is reasonable, but to do it that way would have required a change in [takeover bid] rules, and that is the jurisdiction of the FSA. The FSA and METI, they are competitive."[77] Curtis Milhaupt claims that Delaware corporate law is more familiar to many Japanese lawyers: "For elite Japanese corporate lawyers as well, most of whom received graduate legal education in the United States and are members of the New York or California bars, the transplantation of Delaware takeover law, particularly the need to adapt the poison pill to the domestic legal regime, represents a substantial new business opportunity."[78] Finally, Japanese managerial interests were well represented on the group, and Delaware law favors managers far more than the UK City Code. "Thus, Delaware takeover law provided the METI and Ministry of Justice planners with the best of all possible worlds: a familiar and politically attainable 'global standard' that is somewhat protective of management."[79]

One group that was unhappy with the outcome of the Corporate Value Report was the institutional investors identified in coalitional theory as the likely leaders of reform. The most important political representatives of foreign institutional investors in Japan are the American Chamber of Commerce in Japan (ACCJ) and the European Business Council Japan (EBC). We might have expected the Americans to rejoice over the triumph of Delaware law, while the Europeans bemoaned it. But that is not what happened. Both lobbying groups

[76] Milhaupt (2005: p. 49).
[77] Interview, member of the Corporate Value Study Group, May 16, 2007.
[78] Milhaupt (2005: 51–52), Osugi (2008).
[79] Milhaupt (2005: 50).

launched identical warnings, that adopting Delaware law without Delaware legal infrastructure favored managerial entrenchment.

> [T]he ACCJ is concerned that the sudden and hurried enabling of a broad menu of new takeover defenses, occurring without simultaneous strengthening of legal requirements for corporate governance practices that provide an essential counterbalance, may . . . threaten the equal protection of shareholders, lead to abuse of discretion by 'insider' boards, and result in disputes regarding the ultimate legality of various 'defense' mechanisms.[80]

On release of the report, the EBC urged the government not to "give in to pressure to include comprehensive defensive measures of the Delaware type to prevent greenmailing. Within the Japanese context, these measures would risk a virtual stranglehold on the M&A market and, therefore, on FDI."[81]

The ACCJ and the EBC are lobbying groups used to fighting in legal forums and defending their interests there. And the post-Livedoor boost in political salience had given the release of the report a very high profile, which might have helped their cause. As Hideki Kanda, the group's chair, told me,

> When Livedoor happened we went from being a quiet study group, producing something like a research report, a dissertation, to being very well known, even famous. Livedoor was an unfortunate case for us: at that time, Livedoor was considered the good guy. What Nippon Broadcasting did to defend itself was bad. We were designing takeover defenses, but not of the sort they were using.[82]

The EBC in its statement called on the Japanese government not to adopt the suggestions of the Corporate Value Study Group. The government never did adopt the report, but it did not have to *adopt* the report. Simultaneously with the final release of the group's report in May 2005, METI and MoJ released a set of guidelines over appropriate takeover defenses in the Japanese context.[83] These guidelines spelled out the legal understandings of acceptable takeovers that flowed from the Corporate Value Report. The guidelines spelled out by METI and MoJ did not have the force of law, as they had neither been decided by a court nor adopted by a legislature:

> The Guidelines are not legally binding and should not be read to require that all legitimate takeover measures must conform to the Guidelines. But, if the Guidelines are shared and respected by interested parties including

80 ACCJ (2005: 2–3). The ACCJ, in its detailed public commentary on the first draft of the report, prefaced its statement with a critique of the "excessively tight and narrow time frame between publication of the 130-page . . . report on April 22 and the announced deadline for public comments on May 11 [2005]." (ACCJ 2005: 1)

81 EBC (2005b: 2).

82 Interview with Hideki Kanda, Chair, Corporate Value Study Group, and Professor of Law at the University of Tokyo, June 5, 2007.

83 Osugi (2008).

corporate managers, shareholders, investors, stock exchanges, lawyers, and financial advisors, they will facilitate a major change in the Japanese business community and lead to the enhancement of corporate value.[84]

The guidelines based on the report simply became the uniquely accepted standard about what the Japanese would permit in defending against hostile takeovers. Four months after releasing the report and the guidelines, METI surveyed Japanese corporations about their familiarity with and plans to use the guidelines. Top executives in ninety-six percent of the corporations surveyed said they would use the guidelines if they were planning to adopt hostile takeover defenses. Between the report's release in May 2005 and April 2008, 410 listed companies adopted takeover defenses of the sort discussed in the Corporate Value Report and the METI/MoJ guidelines.[85] One member of the Corporate Value Study Group, whom I interviewed two years after the release of the report, explained the impact of the report and the associated METI guidelines this way:

> In the U.S., I know companies think that anything that is not prohibited is allowed. Japanese companies are the reverse – they think anything not allowed explicitly is prohibited.... [Now] it is a standard. This is only one standard; it is not the same as the Tokyo Stock Exchange's standards, or others. But it is the observed standard. Companies like to say in their press release, they are adopting the METI standards.[86]

The standard by which hostile takeovers would be adjudicated thus emerged from a group in which the most important coalitional opponents of protection, institutional investors, were absent.[87]

[84] METI/MoJ 2005: 2.

[85] Osugi (2008); interview, Director of Corporate System Division, METI, April 25, 2008. This constitutes slightly more than ten percent of all listed firms in Japan. More than three-quarters of these defenses were "advance warning" rights plans, which dilute the power of a potentially hostile acquirer when triggered. The advance warning plan follows the central line of the corporate value report by forcing a would-be acquirer to reveal its postmerger business plan (Osugi 2008). This is the information used by independent committees or boards to determine whether an acquisition plan will contribute to building corporate value.

[86] Interview, member, Corporate Value Study Group, May 16, 2007. The head of a corporate strategy at a large financial holding company, when asked about the importance of the Corporate Value Report for designing takeover protection, told me "this is like the Bible.... I have a copy on my desk." (Interview, senior executive at Millea Holdings, April 15, 2007).

[87] The protests of the institutional investors were eventually acknowledged by the formation of a second "Corporate Value Study Group," with expanded membership (plus all the original members), in September 2005. This group added several financial sector representatives, including notably Tomomi Yano, head of the most important and activist pension fund in Japan, the Pension Fund Association (PFA). Yano has worked closely with activist American funds like CalPERS to bring the principle of shareholder primacy to Japan, and in this light he criticized the original task of the CVSG (Jacoby 2007; interview with Satoshi Kusakabe, METI, convenor of the Corporate Value Study Group, June 26, 2007). The second group published its findings, which dealt mainly with the principles for disclosure of hostile takeover regulations and shareholder/management relations, in March 2006.

The METI guidelines, together with the Corporate Value Report, rapidly established common knowledge among players in the market for corporate control about the new rules of the game.[88] In the process of institutional change, the emergence of common knowledge is an important sign of institutional consolidation because it creates shared understandings about what moves are fair and what moves are not.[89] Once players agree on the rules, they can go back to playing the game and take the rules as given. Once established, common knowledge is sticky; it cannot be unilaterally changed.[90] By creating common knowledge about the new rules of the Japanese hostile takeovers in the absence of institutional investors, the Corporate Value Working Group locked in a set of rules that paid more heed to the concerns of the Keidanren than to those of institutional investors. It enshrined the standard for acceptable takeovers as those that are "fair and reasonable" – that is, those takeovers built on the strategic logic of restructuring firms rather than the market logic of maximizing shareholder value. This was a logic that was consistent with the changes that the managerial organization had favored in corporate law earlier in the decade, in terms of using the takeover market to give firms more tools to reorganize themselves.[91] But it also established the principle that not all takeovers were to be allowed in the new regime of corporate control.

The Corporate Value Report was neither a creation nor an initiative of the managerial lobby. Its members included some of the most prominent experts dealing with corporate law in Japan alongside substantial managerial representation. As an informal group convened by METI, though, it provided a favorable venue for takeover protections to be developed that took account of managerial interests. It was a forum that could exclude institutional investors and other shareholders' representatives because there were no legal requirements of which societal interests must be included. The fact that managers, and the Keidanren itself, were well represented in the group, allowed them to present their views and may indeed have changed the way that other, nonmanagerial representatives presented their own opinions to the group.[92] Even when opponents such as the ACCJ and the EBC mobilized, they were able to have little impact on the takeover guidelines, because the guidelines did not have to be passed in parliament to have an effect. In the vacuum of existing jurisprudence on hostile takeovers, the administrative guidelines of METI quickly became the established rules of the game. These were rules of the game which coalitional actors outside the CVSG were unable to influence.

88 Culpepper (2008).
89 Aoki (2001).
90 Culpepper (2008).
91 Vogel (2006), Schaede (2008).
92 One expert nonmanagerial representative told me, "It was important for me to present myself as one of the professionals, not as a representative of [my company]. [My company] is a big company in the Keidanren, and I did not want to present some view and then have the other members of business take it to the chairman of [my company]" (interview, member, Corporate Value Study Group, May 16, 2007),

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Formal Governance under High Salience: Triangular Mergers

The struggle between the Keidanren and the representatives of foreign investors, the EBC and the ACCJ, was simultaneously taking place on two fronts in 2005. The second front in this conflict was the formal arena, over the law governing triangular mergers. The liberalizing coalition included the institutional investors and one of the most high-ranking and outspoken proponents of increasing FDI in the LDP, Yasuhisa Shiozaki.[93] In this high salience struggle, the managerial lobby lost: the Keidanren obtained a one-year delay in its implementation, but failed to stop the amendment's ultimate adoption. Business actors were unable to compel politicians and bureaucrats adopt their ideal legislation. However, the strong position of the business lobby within the ruling party, the LDP, enabled it to extract some concessions from the reformist coalition. This legal struggle unfolded within a political party and within the formal consultative groups of the bureaucracy. Business lobbying is still an important asset in such venues. But business domination is unlikely because political parties are more interested in responding to the public when the public actually cares about an issue.

Triangular mergers are operations by which a corporation creates a subsidiary, which then merges with a third company. The subsidiary corporation could use shares of the parent company as consideration in the merger. Their essential purpose was to create a legal structure by which foreign companies could use stock swaps, rather than cash, to acquire interested Japanese companies. This was a provision of the corporate law reform which had initially been favored by the Keidanren as a useful tool for company restructuring. Following the UFJ/Sumitomo conflict in 2004, when the Keidanren came out in favor of defenses against hostile takeovers, it also turned against triangular mergers as a potential threat to Japanese companies from foreign predators:

> Through such triangular mergers, a company could acquire a target company with a corporate culture totally different from that of the acquiring company by making a subsidiary merge with the target company. By providing the target company's shareholders with the acquiring company's stocks, instead of the merging company's stocks, the acquiring company can obtain 100 percent of the target company's stocks without paying any cash. Under the above mentioned situation, it cannot be denied that there is a growing risk that buyers who make no long-term commitment to corporate operations would pursue short-term profit for themselves, thereby harming corporate value and causing detriment to shareholders, employees, local communities, and other stakeholders.[94]

It was in this document that the Keidanren first linked the question of triangular mergers and hostile takeovers.

[93] Tiberghien (2007).
[94] Keidanren (2004).

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The link between hostile takeovers and the triangular merger was also made explicitly in the Corporate Value Report in 2005. Technically, a triangular merger requires board approval and so cannot be undertaken against the vote of the board of the company to be acquired. However, the Corporate Value Report underlined that the triangular merger could be used in combination with a tender offer and a proxy fight, as a proxy fight allows an acquiring company to change the composition of management or the board of directors:

> In such cases, the hostile acquirer first buys up shares through TOB (tender offer) and replaces top management, and then conducts the merger, exchange of shares, triangular merger, capital tie-up, or transfer of business. For instance, in the case where the hostile acquirer makes the target a wholly owned subsidiary, it conducts TOB in the first stage and after that, it uses the system of exchange of shares (for M&A among Japanese companies) or the system of triangular merger (in the case where a foreign company makes a Japanese enterprise a wholly owned subsidiary).[95]

By this circuitous route the Keidanren was able to link triangular mergers to hostile takeovers. In response, the EBC and the ACCJ both explicitly pointed out that the triangular merger could only be used in friendly transactions, and that the ballyhooed "wave" of foreign hostile takeovers would simply not appear.[96] Nevertheless, the legislature approved a one-year delay in the implementation of the triangular merger law, from May 2006 to May 2007.

There were two issues at stake on triangular mergers. First, the Keidanren favored extraordinary measures to secure approval from stakeholders of a triangular merger. These extraordinary measures, if passed, would have made approval of triangular mergers effectively impossible.[97] On this issue, the MoJ sided with the institutional investors against the Keidanren, in using the same standard of shareholder approval required by domestic mergers.[98] The second issue involved the ability to secure tax deferral on shares exchanged through a triangular merger.[99] In Japanese law, tax deferral is granted on the condition that a merger creates synergies between the target company and the acquiring company. In its original draft, submitted to the Ministry of Finance (MoF)

95 METI (2005: 31).

96 ACCJ (2005); EBC (2005a and b).

97 The battle turned on the seemingly technical difference is between a *tokusu ketsugi* and *tokubetsu ketsugi* form of shareholder approval. The former measure, favored by the Keidanren for the case of triangular mergers, requires approval of fifty percent of all shareholders (by head, not by voting share), and also by two-thirds of the outstanding shares. The latter form of shareholder approval, which is the one applied in domestic mergers, requires the much less demanding standard of two-thirds of the shares voted at a meeting with at least fifty percent of all shareholders present (Benes and Katsuyama 2006).

98 Interview, senior official involved in triangular merger negotiations, June 8, 2007; interview, ACCJ representative, June 22, 2007.

99 If taxes on capital gains are levied during a share swap – i.e., as though the shares had been converted to cash – this would limit the appeal of the stock swap merger for shareholders. Thus the ACCJ and the EBC lobbied consistently to ensure tax deferral (EBC 2005b: 5).

by METI, those synergies could be considered between an acquiring company (based abroad) and the Japanese company being acquired. Lobbying through the LDP committee that oversees METI, the Keidanren was able to convince lawmakers to submit to MoF a revised version of the law under which the synergies could only take place between a Japanese subsidiary of the acquiring company (if based abroad) and the Japanese target company.[100] The EBC and ACCJ both denounced the change, saying that "new investors in Japan's market effectively would not be able to use the scheme."[101] At least partly in response to these claims, the MoF released a clarifying ordinance in April 2007, applying a nondiscriminatory framework for application between foreign and domestic companies.

In the triangular merger case, which was contested under conditions of high salience, organized managers were unable to block the adoption of the law on triangular mergers on the terms favored by the reformist coalition, which would allow foreign companies to use the measure. Unlike in the CVSG case, the ultimate decisions were taken by lobbying the ruling party directly. Under high salience, parties have more incentive to intervene, and the Keidanren has allies in the conservative wing of the LDP. Relying on these allies, managers achieved a procedural victory by having the party change the terms of tax treatment under the law. This small victory on tax treatment was largely vitiated by the MoF's interpretive framework, which was supported by Shiozaki and the reformist group within the LDP and made the measure accessible to non-Japanese companies. Even under high salience, the close alliance between organized business and the ruling party were important in extracting concessions from liberal reformers. The important point is that under such conditions of sustained high salience, which the issue of hostile takeovers achieved in Japan following the Livedoor attempted takeover, business needs allies to win. It is under these conditions a powerful interest group, but it is still just an interest group.

Conclusion

Driven by the restructuring imperatives facing many large Japanese companies in the depths of the lost decade, organized managers were a powerful force behind the reform of Japanese corporate law from 1997 to 2004.[102] To push through these reforms, they allied with both foreign institutional investors and neoliberal reformers in the ruling LDP and the bureaucracy.[103] This was a powerful coalition for reform, to be sure. As a causal matter, though, this alliance of convenience obscures the relative influence of the three groups over

[100] EBC (2006); interview, senior official involved in triangular merger negotiations, June 8, 2007.

[101] EBC (2006). The Keidanren fired back, warning that "allowing foreign interests to meddle in the revision of our country's tax system should be cause for alarm" (ACCJ 2006).

[102] Vogel (2006), Shishido (2007), Schaede (2008).

[103] Gilson and Milhaupt (2004), Tiberghien (2007), Ahmadjian (2007).

the institutions of corporate governance. And for most of the period, organized managers were the dominant players in this coalition. When they broke with other members of the coalition, as in the 2002 reform of corporate structure, they succeeded in imposing their preferred outcome on the other members of the reformist coalition.

To understand why Japanese managers acquiesced in the breakdown of cross-shareholdings in an earlier period, but then later mobilized to adopt a system of hostile takeover protections in 2005, it is necessary to understand variations in their perception of the threat posed by an active market for corporate control. The Keidanren is an organization dominated by large firms. Those large firms aggressively reorganized in order to focus on their core business at the end of the 1990s.[104] The weakness of Japanese firm-level employee representation meant that workers were in no position to halt such reorganizations. The possibility of hostile takeovers is one that these managers were willing to accept in their attempt to return to economic growth after the lost decade, and indeed they viewed a more active market for corporate control as a potentially beneficial tool of reorganization. Beneficial reorganization looks especially helpful when it happens to someone else, and the attempted hostile takeovers that took place prior to 2004 affected only small companies, not large ones. The battle over UFJ, for which Sumitomo launched an ultimately failed hostile bid, was the first instance in which large firms at the center of the Japanese economy seemed to be at risk of hostile takeover. Livedoor's unconventional bid for Fuji TV, through its attack on NBS, triggered even more widespread concern about the threat of hostile takeovers. After 2005, the reformist coalition, which had previously included LDP reformers, institutional investors, and organized managers, ceased to exist. It was replaced by a series of battles pitting these former allies directly against one another.

The deliberations of the Corporate Value Study Group (CVSG) established a set of rules to govern the newly active Japanese market for corporate control. The managerial community had been uninterested in the CVSG when it was first convened by a METI bureaucrat in the spring and summer of 2004. The group was not a Keidanren initiative, but its composition favored managers and disadvantaged managerial opponents, notably excluding any institutional investors or labor representatives. When the Livedoor event occurred, bringing concentrated public attention to the issue of corporate control, the group was already in place and moving toward publication of its final report. The CVSG allowed managers and experts to deliberate in an informal group without legislative oversight or public scrutiny. The group's findings, which were published simultaneously with METI/MoJ guidelines for hostile takeovers, created a new standard for acceptable hostile takeover protections without ever needing to be passed into law. By creating common knowledge among Japanese companies of the new acceptable practices of takeover protection, this informal group

[104] Schaede (2008).

set the new rules of corporate control for Japanese companies, which would henceforth be adjudicated in the formal arena of courts. The arrangements adopted resembled those of the American state of Delaware, and like those of Delaware, they were highly protective of managerial prerogatives.[105]

Managers fared less well in the battle over the triangular merger amendment because it was decided in the formal political arena after hostile takeovers had acquired high political salience with the general public. The Keidanren attempted to impose onerous conditions of shareholder approval and tax deferral, conditions that would effectively have eliminated the ability of foreign companies to use triangular mergers in Japan. The Keidanren was defeated on this issue. The managerial organization scored a limited victory on taxation within the committees of the ruling party, which is where high salience battles are likely to be decided. However, its victory on taxation was heavily diluted by an ordinance drafted by MoF and supported by the reformists within the LDP to render the clause nondiscriminatory between Japanese and foreign firms.

The Japanese political system remains favorable to the protection of managerial interests, given the long and close ties among business, the bureaucracy, and the Liberal Democratic Party.[106] Thus, even on high salience issues, it would be surprising if Japanese managers were unable to exercise important political influence. The theory of quiet politics leads us to expect that the effectiveness of different tools of business influence varies according to political salience. The Corporate Value Study Group, which was constituted before hostile takeovers reached general public attention in Japan, provided a forum for rule making that was congenial to managerial interests. Such informal groups, or *shingikai*, have long been used by Japanese bureaucrats for the purpose of evading legislative oversight. Because the group had already been established by the time of the Livedoor event, it was able to lay down the new rules of the game without throwing the issue into the formal arena of the Diet. The triangular merger law, in contrary fashion, was decided by politicians through a battle between conflicting factions of the LDP. The sustained high salience of the issue meant that political party actors were much keener to intervene on it in defense of their respective constituencies. It was only in such a public battle, with close allies in the ruling party, that institutional investors were able to score points against organized managers in political battles over Japanese corporate control. The future functioning of the new rules of corporate control in Japan, which provide an important role for oversight of takeover activity by courts, will likely depend on whether the issue continues to be one of high salience. If it does not, the dynamics of quiet politics will reassert themselves and these dynamics do not favor interest groups that oppose the managers of large companies.

[105] Milhaupt (2005), Osugi (2008).
[106] Vogel 2006, Hamada (2010).

Appendix 5.1: Roster of the Corporate Value Study Group (2004–2005)

Chairman

Hideki KANDA Professor, University of Tokyo Graduate Schools for Law and Politics
Toshio ADACHI Corporate Director, Group General Manager, Tokyo Branch, Sharp Corporation
Gaku ISHIWATA Attorney at Law, Mori Hamada & Matsumoto
Takeki UMEMOTO Executive Officer, Director, Information Planning Department, RECOF Corporation
Toshio OSAWA Corporate Officer, Corporate Administration Division Head, Astellas Pharma Inc.
Kenichi OSUGI Professor, Chuo Law School
Masakazu KUBOTA Director, Economic Policy Bureau, Japan Business Federation Nippon
Nobuo SAYAMA Professor, Graduate School of International Corporate Strategy, Hitotsubashi University, CEO, GCA CO., LTD.
Kazufumi SHIBATA Professor, Hosei University Law School
Kazuhiro TAKEI Attorney at Law, Nishimura & Partners
Shirou TERASHITA Executive Officer, IR Japan, Inc.
Motoyoshi NISHIKAWA Chief Legal Counsel, Nippon Steel Corporation
Takashi HATA Managing Officer, Finance & Accounting Group, Toyota Motor Corporation
Nobuo HATTA Member of the Board, Director, Administrative Headquarters, ROHM Co. Ltd.
Takashi HATCHOJI Senior Vice President and Executive Officer, Hitachi, Ltd.
Kenichi FUJINAWA Attorney at Law, Nagashima, Ohno & Tsunematsu
Keisuke HORII Senior Vice President, Global Hub Compliance Office, Sony Corporation
Nami MATSUKO Director, Investment Banking Consulting Dept, Nomura Securities Co., Ltd.
Eizo MATSUDA Editorial Writer, Yomiuri Shimbun
Toshikazu MURATA Division Counselor, Planning and Research Division, Nippon Life Insurance Company

Division Counselor, Planning and Research

Noriyuki YANAGAWA Associate Professor, Graduate School of Economics, Faculty of Economics, The University of Tokyo

(Observer)

Tetsu AIZAWA Secretary, Civil Affairs Bureau, Ministry of Justice