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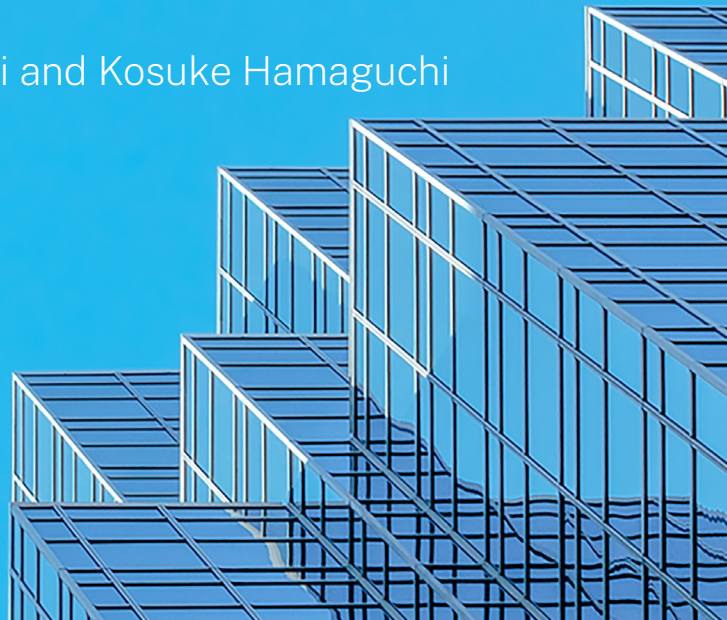
# Corporate Governance 2025

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## **Japan: Law and Practice**

Hiroshi Mitoma, Tomohiko Iwasaki and Kosuke Hamaguchi  
Nagashima Ohno & Tsunematsu



# JAPAN

## Law and Practice

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**Nagashima Ohno & Tsunematsu** has an established reputation as a leading Japanese law firm in the area of corporate governance. With a team of approximately 75 partners, having various backgrounds ranging from corporate/M&A and capital markets to litigation and investigations, the firm regularly advises on corporate governance matters. It provides practical and strategic advice related to corporate governance based on relevant laws, regulations and guidelines as well as current practices. The key areas of the firm's practice in the corporate

governance sector include conduct of shareholder meetings; proxy statements, securities reports and other disclosure materials; investor relationships; dealing with shareholder activists; management composition and governance structure; management compensation; internal control systems; risk and crisis management; and fiduciary duties, the business judgment rule and directors' liability. The firm primarily advises listed companies in the corporate governance context, but from time to time advises institutional investors as well.

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## 1. Introductory

### 1.1 Forms of Corporate/Business Organisations

The following are the principal forms of corporate/business organisations in Japan. Explanations found in **1.2 Sources of Corporate Governance Requirements** and later sections focus on the joint stock company unless otherwise indicated.

#### Joint Stock Company (Kabushiki Kaisha or KK)

A joint stock company is the most commonly used form of corporate/business organisation in Japan. All Japanese listed companies are joint stock companies. This form is commonly used for closely held companies as well. All shareholders of a joint stock company enjoy limited liability up to their respective contribution amounts. This form is not a pass-through entity for Japanese tax purposes.

#### Limited Liability Company (Godo Kaisha or GK)

The form of a limited liability company is used only for closely held companies. The governance structure and rights of equity holders (including the allocation of profit distributions among equity holders) can be determined in a flexible manner by the articles of organisation, so this form is suitable for joint ventures and wholly owned subsidiaries. All equity holders of a limited liability company enjoy limited liability up to their respective contribution amounts. This form is not a pass-through entity for Japanese tax purposes.

#### General Partnership Company (Gomei Kaisha) and Limited Partnership Company (Goshi Kaisha)

The form of a general partnership company and that of a limited partnership company are used only for closely held companies, but are not commonly used. General partners in these companies have unlimited liability; limited partners enjoy limited liability. These forms are not pass-through entities for Japanese tax purposes.

#### Limited Liability Partnership (LLP)

The form of a limited liability partnership is used for joint ventures. The number of limited liability partnerships has been increasing but, despite its pass-through nature for Japanese tax purposes, has not become very popular because of some practical inconveniences arising from its lack of legal personality.

### 1.2 Sources of Corporate Governance Requirements

There are various sources of corporate governance requirements for companies in Japan. The following are the principal sources.

#### Companies Act (Act No 86 of 2005, as Amended)

The Companies Act, together with its subordinate regulations, provides the basic corporate governance requirements for companies, whether listed or not. The latest major amendment was made in December 2019.

#### Financial Instruments and Exchange Act (Act No 25 of 1948, as Amended) (FIEA)

The FIEA, together with its subordinate regulations, requires listed companies and certain other publicly held companies to make disclosures related to corporate governance in various filings.

## Securities Listing Regulations Published by the Tokyo Stock Exchange (TSE Regulations)

The TSE Regulations include certain corporate governance requirements which companies listed on the Tokyo stock exchange must comply with. The Tokyo stock exchange has three segments (Prime, Standard and Growth). Companies listed at the Prime Market must meet enhanced corporate governance requirements. Companies listed at the Prime Market, the Standard Market and the Growth Market respectively account for approximately 43%, 41% and 16% among approximately 3,800 companies listed at the Tokyo stock exchange as of April 2025.

## Corporate Governance Code

The Corporate Governance Code is a part of the TSE Regulations. The Tokyo stock exchange requires listed companies to “*comply or explain*” with respect to the principles included in the Corporate Governance Code and to disclose some corporate governance matters in their corporate governance reports. The latest amendment to the Corporate Governance Code took effect in June 2021.

## Stewardship Code

The Stewardship Code published by the Council of Experts on the Stewardship Code, established by the Financial Services Agency, is another source of important corporate governance requirements, although it is not directly applicable to listed companies but to institutional investors. The Stewardship Code of 2020 is the most recent version. Many major institutional investors have published their own proxy voting policies in response to the Stewardship Code, will vote at shareholder meetings in accordance with their own policies, and will have engagement discussions with the management of listed companies to encourage mid- to long-term growth.

## Guidelines and Study Reports

Japanese governmental agencies or study groups organised by them from time to time publish various guidelines or study group reports with respect to corporate governance issues, which include the Corporate Governance System Guidelines, the Fair M&A Guidelines, the Outside Directors’ Guidelines and the Guidelines for Corporate Takeovers.

## 1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Listed companies are subject to various corporate governance requirements, including the following.

### Governance Structures

Having a board of directors is mandatory. Listed companies must choose one of the three governance structures:

- company with a board of statutory auditors;
- company with an audit and supervisory committee; or
- company with nominating and other committees.

Companies with a board of statutory auditors, companies with an audit and supervisory committee, and companies with nominating and other committees respectively account for approximately 55%, 43% and 2% among approximately 3,800 companies listed at the Tokyo stock exchange as of April 2025.

### Outside/Independent Members

All the listed companies are required to have outside director(s) under the Companies Act.

The Corporate Governance Code provides that one third or more of the directors should be inde-



pendent outside directors in the Prime Market (or two or more directors must be independent outside directors in the other markets). If a listed company has a controlling shareholder, enhanced requirements regarding independent outside directors will apply in order to protect the interest of minority shareholders.

### Shareholder Proposal Right

Shareholders who hold 1% or more of the total voting rights or 300 or more of the votes for six months or longer may make a proposal of up to ten agenda (including appointment and dismissal of directors) by notifying the company at least eight weeks (or a shorter period if so provided in the articles of incorporation) prior to a shareholder meeting.

## 2. Corporate Governance Context

### 2.1 Hot Topics in Corporate Governance

In December 2023, the Financial Services Agency amended the subordinate regulations under the FIEA to enhance disclosure requirements related to:

- agreements between a listed company and its shareholder regarding the governance (eg, director nomination right);
- agreements between a listed company and its major shareholder regarding disposal or additional acquisition of shares (eg, standstill); and
- financial covenants included in loan agreements or bond indentures.

Most of these amendments became applicable from April 2025.

In February 2024, the Tokyo stock exchange issued a notification which requires companies

listed at its Prime Market to make public disclosures in English (in addition to Japanese), effective from April 2025.

Recent significant increase of shareholder activism and hostile takeovers in Japan reveals that some updates and reforms are necessary in the regulations regarding the takeover bids and the bulk shareholding reports in the FIEA. In May 2024, the Diet passed the amendment to the FIEA to reform the rules for takeover bids and the bulk shareholding reports. These amendments are expected to become applicable in 2026. Draft amendment to the Stewardship Code is being reviewed taking into account this amendment to the FIEA.

The Legislative Council of the Ministry of Justice started to discuss amendment to the Companies Act, which is to cover some corporate governance issues, including:

- introduction of virtual/online shareholder meetings;
- introduction of the system for confirming the identity of beneficial owners; and
- amendment to the rules applicable to companies with nominating and other committees.

### 2.2 ESG Considerations

The Corporate Governance Code suggests that a listed company:

- take appropriate measures to address sustainability issues, including social and environmental matters;
- develop a basic policy for the company's sustainability initiatives from the perspective of increasing corporate value over the mid- to long-term; and
- appropriately disclose its initiatives regarding sustainability in its management strategies



and provide information on investments in human capital and intellectual properties.

In particular, a listed company on the Prime Market is encouraged to collect the necessary data to analyse the impact of the risks and earning opportunities related to climate change on its business activities and profits and to enhance the disclosure based on the Task Force on Climate-related Financial Disclosures (TCFD) recommendation or an equivalent framework.

Under the FIEA, publicly traded companies (in this context, listed companies and other companies that are required to file annual securities reports under the FIEA) are required to disclose their notion and efforts on sustainability in annual securities reports. This disclosure requirement spans the following four categories:

- governance;
- strategy;
- risk management; and
- indexes and goals.

In addition, in response to the establishment of the inaugural global sustainability disclosure standards (IFRS S1 and IFRS S2) by the International Sustainability Standards Board in June 2023, the Sustainability Standards Board of Japan established the sustainability disclosure standards (the “SSBJ Standards”) in March 2025. The SSBJ Standards, which can be applied voluntarily at this point, are expected to be adopted in the legal disclosure regime.

## 3. Management of the Company

### 3.1 Bodies or Functions Involved in Governance and Management Shareholder Meeting/Directors/Board of Directors

All joint stock companies are required to have a shareholder meeting and directors. If a company has a board of directors, it must appoint three or more directors. A listed company is required to have a board of directors. A company may have one of the following bodies:

- a statutory auditor and, as the case may be, a board of statutory auditors;
- an audit and supervisory committee; and
- nominating and other committees.

If a company has any of a board of statutory auditors, an audit and supervisory committee or nominating and other committees, it must also have a board of directors. A listed company that is a large-sized company (*daigaisha*), ie, a company that has recorded on its audited and approved balance sheet for its most recent fiscal year either JPY500 million or more in stated capital, or JPY20 billion or more in liabilities, is required to have one of these bodies.

#### Statutory Auditors

The main role of a statutory auditor is to audit the execution of the duties of the directors. A listed company with statutory auditors is required to have a board of statutory auditors.

#### Audit and Supervisory Committee

An audit and supervisory committee consists of three or more audit and supervisory members, who are also directors of the company elected as such by its shareholder meeting. A majority of the audit and supervisory members must be outside directors. The main role of the audit and

supervisory committee is to audit and supervise the execution of the duties of the directors.

### Nominating and Other Committees

Nominating and other committees means a set of a nominating committee, an audit committee and a compensation committee. Each committee consists of three or more directors, and a majority of each committee's members must be outside directors. The main roles of a nominating committee, an audit committee and a compensation committee are, respectively, to determine the candidates for directors, to audit and supervise the execution of the duties of the management, and to determine the compensation of each management member.

In a company with nominating and other committees, an executive officer is supposed to have the broader authority to decide the execution of the company's operation as compared to other types of companies. A representative executive officer appointed from among the executive officers by a board of directors represents the company.

### Accounting Auditor

In addition, a large-sized company must have an accounting auditor who is expected to audit the accuracy of the company's financial statements. An accounting auditor must be appointed from among external accounting firms or licensed accountants. A company with an audit and supervisory committee or nominating and other committees is also required to have an accounting auditor.

## 3.2 Decisions Made by Particular Bodies

The roles of a shareholder meeting and directors may differ depending on whether or not a company has a board of directors. In the case of a company without a board of directors, a

shareholder meeting may adopt any action on behalf of the company, and a director has the broad authority to decide and execute the company's operation.

If a company has a board of directors, the authority of a shareholder meeting is more limited. In this case, the shareholder meeting may adopt only such matters as provided under the Companies Act or the articles of incorporation. A board of directors typically delegates to the representative director and other executive directors the authority to decide the execution of the company's operation except for the matters specifically prescribed under the Companies Act.

### Monitoring Model Approach

However, in the case of a company with nominating and other committees, a board of directors may delegate to the executive officer the broader authority to decide the execution of the company's operation, and the matters that the board of directors is required to decide are fairly limited as compared to other types of companies. In this sense, the corporate governance of a company with nominating and other committees is designed as a monitoring model. Likewise, a company with an audit and supervisory committee may take a similar approach if:

- a majority of its directors consist of outside directors; or
- it is so provided in the articles of incorporation.

## 3.3 Decision-Making Processes

At the board level, unless otherwise provided in the articles of incorporation, a decision by a board of directors is made by a majority of the directors present at a board meeting, as long as a majority of the directors who are entitled to participate in the vote are present. Directors who

have a special interest in the resolution may not participate in the vote. A board meeting may be held through a video-conference or conference call system.

If so provided in the articles of incorporation, a board resolution may be made without holding a physical meeting if all directors who are entitled to participate in the vote agree in writing (whether physically or electronically) to a proposal submitted by a director. That being said, circulation of board minutes to the board members together with their signatures on the minutes is not deemed to be a board resolution.

## 4. Directors and Officers

### 4.1 Board Structure

A board of directors consists of three or more directors and is required to appoint one or more representative directors. In the case of a joint stock company with an audit and supervisory committee or nominating and other committees, a majority of each committee's members must be outside directors.

In the case of a company with nominating and other committees, members of each committee may serve as members of other committees.

### 4.2 Roles of Board Members

The board members are, in general, divided into the following categories:

- representative directors;
- other executive directors; and
- outside directors.

#### Representative Directors

The role of the representative director is to execute the company's operation and represent the

company. The authority of the representative director extends to all actions (whether judicial or non-judicial) in connection with the company's operation. The representative director may also decide the company's operation to the extent permitted by law as long as the board of directors authorises them to do so.

#### Other Executive Directors

Other executive directors may not represent the company without a delegation from the representative director but may decide and execute the company's operation, as is the case with a representative director subject to the same condition. However, in the case of a company with nominating and other committees, directors (other than executive officers) are not generally allowed to decide and execute the company's operation because such functions are carried out by an executive officer.

#### Outside Directors

Outside directors are expected to supervise the management of the company from an independent point of view.

### 4.3 Board Composition Requirements/Recommendations

A company with an audit and supervisory committee or nominating and other committees must have two or more outside directors. There are several requirements or recommendations for listed companies.

- First, a listed company with a board of statutory auditors is obligated to have one or more outside directors under the Companies Act.
- Second, the Corporate Governance Code recommends that:
  - (a) listed companies on the Prime Market ensure that one third or more of their

directors are independent outside directors; and

- (b) other listed companies appoint at least two independent outside directors.
- Third, the TSE Regulations require listed companies to make efforts to secure at least one independent outside director as a board member.

In addition, the Corporate Governance Code recommends that a board of directors of a listed company be composed in a manner to achieve diversity, including in terms of gender, international experience, work experience and age.

## 4.4 Appointment and Removal of Directors/Officers

### Appointing Directors

Directors are appointed by a resolution of a shareholder meeting. Unless otherwise provided in the articles of incorporation, this resolution must be made by a majority of the votes of the shareholders present at the meeting if a quorum is satisfied (ie, by the presence of shareholders representing a majority of those who are entitled to exercise their voting rights). The company may lower the quorum for the appointment of directors down to a third pursuant to the articles of incorporation.

A cumulative voting system is also available although this is not common in Japan. In the case of a company with an audit and supervisory committee, directors who are audit and supervisory members must be appointed separately from the other directors of the company. Other management members, including an executive officer in a company with nominating and other committees, are appointed by the board of directors.

In addition, the Corporate Governance Code recommends that a listed company, unless it has nominating and other committees or its independent outside directors constitute a majority of its board of directors, seek the involvement of, and advice from, an independent nominating committee regarding the appointment of its directors or other management members. In particular, a listed company on the Prime Market is encouraged to ensure that a majority of such nominating committee's members are independent outside directors and disclose, among other things, the view on the independence regarding the composition of the nominating committee and its authority and roles.

### Qualifications of Directors

Although the Companies Act provides the restrictions on qualification of directors that a corporation cannot be a director or an individual who was sentenced for breaching laws and regulations may not become a director during a certain period, there are no nationality or residence restrictions.

### Dismissing Directors and Other Members of Management

Directors may be dismissed at any time by a majority of the vote at a shareholder meeting, except audit and supervisory members, whose dismissal requires two thirds of the votes at a shareholder meeting. However, a dismissed director is entitled to seek damages arising out of the dismissal except in cases where justifiable grounds exist. Typically, a dismissed director may claim the compensation they would have received during their remaining term.

In addition, if a director engages in any misconduct or commits a material violation of law or the articles of incorporation in connection with the execution of their duties as a director, and a

proposal to dismiss the director is rejected at the shareholder meeting, then a shareholder holding, for the preceding six months or longer, not less than 3% of the voting rights of all shareholders may file a lawsuit to dismiss the director.

Other management members, including an executive officer in a company with nominating and other committees, may be dismissed by a board of directors. A dismissed executive officer may seek damages, as in the case of a dismissed director.

## Statutory Auditors

Statutory auditors are appointed by a majority of the votes at a shareholder meeting. However, dismissal of statutory auditors requires two thirds of the votes at a shareholder meeting. As in the case of directors, a dismissed statutory auditor is entitled to seek damages arising out of the dismissal, except in cases where justifiable grounds exist.

## 4.5 Rules/Requirements Concerning Independence of Directors

An outside director is a director who does not, in principle, execute the company's operations, and has no relationship with its affiliate companies or their management, etc. A more detailed definition of an outside director is provided in the Companies Act.

Furthermore, the TSA Regulations and the Corporate Governance Code have certain requirements or recommendations in relation to "*independent*" outside directors. An independent outside director is an outside director who satisfies the "*independent officer*" criteria as established by the Tokyo stock exchange. According to these criteria, an outside director who is an executive director or officer of one of the company's main business partners, or an expert

who receives a substantial amount of fees or compensation from the company, is not qualified to be an "*independent*" outside director. In this sense, the "*independent officer*" criteria are more stringent than the "*outside director*" criteria under the Companies Act. Under the Corporate Governance Code, if a listed company on the Prime Market does not appoint such a number of independent outside directors as to constitute one third or more of its directors (or if a listed company on other markets does not appoint two or more independent outside directors), it must publicly explain the reason why. Under the Corporate Governance Code, it is also recommended that a person who has experience managing other companies be included among such independent outside directors.

The Corporate Governance Code also suggests that a listed company with a controlling shareholder appoint such number of independent outside directors who are independent of the controlling shareholder as to constitute at least one third of its directors (in respect of a company listed on the Prime Market, a majority) unless the listed company establishes a special committee composed of independent persons, including independent outside directors, to deliberate and review material transactions or matters that involve a conflict of interest between the controlling shareholder and the minority shareholders.

## 4.6 Legal Duties of Directors/Officers

Directors owe a fiduciary duty to the company. The Companies Act specifically provides that directors of a company must perform their duties to the company in a loyal manner, with this duty of loyalty being construed as part of a fiduciary duty. As part of their fiduciary duty, directors are required to establish an internal control system of the company. Furthermore, directors have a

duty to supervise other directors' execution of the company's operation.

In connection with the decision on a company's operation, the business judgement rule applies, whereby directors are given broad discretion in making business decisions and are not to be held liable for those decisions unless the business decision or the process thereof is construed as significantly unreasonable.

If a director intends to carry out any transaction:

- with the company;
- that competes with the business of the company; or
- that results in a conflict of interest between the director and the company,

then the director is required to disclose the material facts relating to the transaction to the board of directors and obtain its approval.

## 4.7 Responsibility/Accountability of Directors

In general, directors owe their duties to the company. However, if a director breaches its fiduciary duty or any other duties, it may be held liable not only to the company but also to any third party that has suffered damage arising from the breach.

## 4.8 Consequences and Enforcement of Breach of Directors' Duties

### Injunctive Relief

If a director engages, or is likely to engage, in an act in violation of law or the articles of incorporation (such acts include breach of a fiduciary duty) and this act is likely to cause substantial damage to the company, a shareholder holding shares in the company for six consecutive months or longer (or a shorter period if so provided in the

articles of incorporation) may seek injunctive relief. In the case of a closely held company, the restriction on the shareholding period does not apply. In the case of a company with statutory auditors, an audit and supervisory committee or nominating and other committees, injunctive relief is granted only if the company is likely to suffer irreparable damage because statutory auditors or the relevant committee members are expected to audit and supervise the directors.

### Compensation for Breaches/Third-Party Claims

If a director or a statutory auditor breaches their duties, the company may seek compensation for the damage caused by the breach. In addition, a shareholder may also file a shareholder derivative action on behalf of the company if the shareholder requests that the company file a lawsuit against a breaching director or statutory auditor but the company does not do so within 60 days of such a request. Moreover, if a third party suffers damage arising from the performance of the duties by a director or a statutory auditor who had knowledge that their conduct was inappropriate or was grossly negligent, then the third party may seek recovery of the damage from the director or statutory auditor.

Even if a director or a statutory auditor fails to perform their duties, their liability to a company arising from such failure may be discharged or limited through:

- the consent of all shareholders;
- a resolution of a shareholder meeting; or
- a resolution of a board of directors (or, in the case of a company without a board of directors, consent of a majority of two or more directors) pursuant to the articles of incorporation.



In addition, a director who is neither a representative director nor an executive director or a statutory auditor may enter into an agreement with a company to limit their liability, if so permitted by the articles of incorporation.

#### Indemnification Agreement/D&O Insurance

A director may enter into a corporate indemnification agreement with a company, pursuant to which in certain circumstances the company indemnifies the director for the costs (including attorneys' fees) and damage that the director has incurred in connection with the performance of their duties. D&O insurance is widely available in Japan. The Companies Act makes clear that in order to enter into a corporate indemnification agreement or D&O insurance, a company needs to obtain an approval of its board of directors or, in case of a company without a board of directors, a shareholder meeting.

#### 4.9 Other Bases for Claims/Enforcement Against Directors/Officers

In relation to corporate governance, a third party is able to make claims against directors, statutory auditors and other officers for damage incurred in connection with misrepresentations in a company's financial statements, business reports or any other documents unless the directors, statutory auditors or other officers can prove that they have exercised due care. Directors, statutory auditors and other officers of a listed company are also liable for misrepresentations in the public disclosure documents of the company, such as annual securities reports, under the FIEA.

#### 4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

##### Compensation to Directors

Compensation to directors must be approved by a shareholder meeting unless it is provided in the articles of incorporation. In usual circumstances, a shareholder meeting approves the maximum aggregate amount of compensation of all directors and delegates to the board of directors the authority to decide the compensation to be paid to each director within the approved maximum aggregate amount. In such a case, the board of directors of a listed company with a board of statutory auditors that is a large-sized company or a company with an audit and supervisory committee must approve the policy as to how to determine the specific amount of compensation of each director and disclose this policy in the annual business report. The authority to decide the compensation of each director based upon this policy is often delegated to a representative director or an independent compensation committee.

If the total amount of the compensation of all directors exceeds the maximum aggregate amount of compensation approved by a shareholder meeting, the compensation in excess of the maximum aggregate amount is invalid. In such case, it is considered that the amount of the compensation of each director would be reduced based on a ratio of the total amount of the compensation of all directors to the maximum aggregate amount approved by a shareholder meeting; and a company has a right to request each director to return the excessive amount regardless of its negligence. In addition, the directors involved in such illegal payment are jointly and severally liable to the company for the amount in excess of the maximum aggregate amount approved by a shareholder meeting.



If a company issues its stock or stock options to its directors as compensation, it also needs to obtain the approval of a shareholder meeting on the maximum number of such stock or stock options to be issued and other prescribed details.

In the case of a company with an audit and supervisory committee, the compensation of audit and supervisory members must be determined separately from other directors, and the allocation of compensation among audit and supervisory members is determined based upon their discussion unless a shareholder meeting resolves otherwise or the articles of incorporation provide differently.

In the case of a company with nominating and other committees, a compensation committee determines the compensation of each director and executive officer.

## Principles Under the Corporate Governance Code

The Corporate Governance Code recommends that a listed company, unless it has nominating and other committees or its independent outside directors constitute a majority of its board of directors, seek involvement of and advice from an independent compensation committee regarding the compensation of its directors. In particular, a listed company on the Prime Market is encouraged to ensure that a majority of such compensation committee's members consists of independent outside directors and disclose, among other things, the view on the independence regarding the composition of the compensation committee and its authority and roles.

The Corporate Governance Code also considers that listed companies should reflect mid- to long-term business results and potential risks in

determining the compensation of the management and recommends that the proportion of management compensation linked to mid- to long-term results and the balance of cash and stock paid as compensation, respectively, be set appropriately.

## Compensation to Statutory Auditors

Compensation to statutory auditors must also be approved by a shareholder meeting unless it is provided in the articles of incorporation. If a company has two or more statutory auditors, compensation of each statutory auditor may be determined based on their discussions, within the maximum aggregate amount of compensation approved by a shareholder meeting or provided by the articles of incorporation.

## 4.11 Disclosure of Payments to Directors/Officers

A listed company must disclose the compensation of its directors, statutory auditors and other officers in its business report. Such disclosure is required with respect to the total amount of the compensation on a position-by-position basis along with the number of persons appointed to each position, if and to the extent that the amount of the compensation of each individual is not disclosed. Where a company has outside directors/statutory auditors, the total amount of the compensation paid to them and the number of such outside directors/statutory auditors must also be disclosed.

Further, a listed company is required to disclose its basic policy, if any, on the determination of the compensation of each director, statutory auditor and other officer. Unless the specific amount of compensation for each director is stated in the articles of incorporation or approved at a shareholder meeting (which is a rare case in practice), the policy as to how to determine the specific

amount of compensation of each director also needs to be disclosed. If the compensation is linked to performance, the KPIs used for the calculation of the amount of such compensation, the reasons for choosing such KPIs or other prescribed details must also be disclosed.

Furthermore, a listed company is required to disclose the compensation of individual directors, statutory auditors and other officers in its annual securities report under the FIEA if the amount of such individual compensation is JPY100 million or more.

In the case of a closely held company, while there is no such disclosure requirement, its financial statements may have to make available the total amount of compensation paid to its directors, statutory auditors and other officers.

## 5. Shareholders

### 5.1 Relationship Between Companies and Shareholders

Shareholders, through their ownership of shares, have equity interests in a joint stock company. The basic and primary rights of shareholders are:

- the right to receive dividends;
- the voting right at shareholder meetings; and
- the right to receive residual assets upon the liquidation of the company.

Shares are issued only upon the full payment of the issuance price by a shareholder; accordingly, there exists no obligation of shareholders to make an additional investment/payment in their capacity as shareholders. Additionally, unlike in some other jurisdictions, it is generally construed that a controlling shareholder does not

owe any fiduciary duty in relation to the operation of the company.

Accordingly, in principle, the risk assumed by shareholders is limited to the equity amount invested in the company. However, in limited circumstances, a doctrine to pierce the corporate veil exists pursuant to court precedent where the benefit of the corporate form is abused or the existence of the corporate form becomes a mere facade.

While there is no publicly available record of the shareholders of a company, a shareholder or a creditor of a company can request inspection of the shareholders register that the company is required to keep under the Companies Act.

### 5.2 Role of Shareholders in Company Management

Shareholders are not directly involved in the management of a company.

Rather, shareholders, in their capacity as members of a shareholder meeting, vote on agenda items presented at the shareholder meeting and make resolutions on such proposed matters. In the case of a company with a board of directors, the shareholder meeting only has the power to make resolutions on the matters stipulated by law or stipulated in the articles of incorporation. Accordingly, it is not expected that a shareholder meeting will make resolutions regarding the day-to-day management of the company.

Once a resolution is passed by a shareholder meeting, the directors of the company owe a duty to act in accordance with such a resolution.

In the case that a director or a company is to take certain actions that are likely to adversely affect shareholders or the company, under limited cir-

cumstances satisfying the criteria stipulated in the Companies Act, a shareholder may demand that the company or director refrain from taking such actions. Additionally, a shareholder may bring a claim against the company or directors as explained in **5.4 Shareholder Claims**.

For the purpose of monitoring the company's management, when satisfying the requirements provided under the Companies Act:

- a shareholder holding 3% or more of the voting rights may request the court to appoint an inspector for the company's business;
- a shareholder holding 3% or more of the voting rights may request the disclosure of the accounting books and related documents of the company; and
- a shareholder may request, with the court's permission, the disclosure of the minutes of meetings of the board of directors.

## 5.3 Shareholder Meetings

### Types of Shareholder Meetings

A company is required to have an annual shareholder meeting once every fiscal year. At an annual shareholder meeting, the financial statements/business reports are approved or reported and annual dividends may be declared. The appointment of directors or statutory auditors may also take place.

The articles of incorporation usually set forth that the shareholders as of the end of the relevant fiscal year will have voting rights at the annual shareholder meeting, and this annual shareholder meeting is required to be held within three months after the end of the relevant fiscal year.

An extraordinary shareholder meeting may be convened from time to time. For a company whose shares may be transferred without restric-

tion (including listed companies), the company must set a record date by giving public notice in order to identify the shareholders who may exercise their voting rights at the relevant shareholder meeting.

Some listed companies are holding a virtual or semi-virtual shareholder meeting by using web conference systems. An amendment to the relevant laws was passed in 2021 that enables a company to have “full” virtual shareholder meeting (ie, a shareholder meeting without a concept of the “venue” of the meeting).

### Convocation Procedure

The convocation of a shareholder meeting by the company is required to be made by a resolution of the board of directors and, in general, a convocation notice is required to be sent out to the shareholders at least two weeks prior to the scheduled date of the shareholder meeting.

In the case of a listed company, the required content of the proxy statements for a shareholder meeting is stipulated in the relevant regulations. From the year 2023, pursuant to the latest amendment to the Companies Act, which was enforced on 1 September 2022, a listed company is required to provide the proxy statements via electronic means at least three weeks prior to the scheduled date of the shareholder meeting. In exchange, it is not legally required to send the proxy statements in printed form unless requested so by a shareholder.

In the case of a closely held company with a limited number of shareholders, if all the shareholders agree to have a shareholder meeting with a shortened notice period, a shareholder meeting may be validly held in accordance with such agreement. Additionally, if all the shareholders approve the proposed agenda unanimously in

writing (or by email), then the resolution of a shareholder meeting will be deemed to have been made without having an actual physical meeting.

Apart from the convocation of a shareholder meeting by the company, a shareholder holding 3% or more of the voting rights may, with the court's permission, convene a shareholder meeting.

### Proposal by a Shareholder

When the company convenes a shareholder meeting, within the scope of an agenda item proposed by the company, a shareholder may make a counter proposal during the meeting. For example, if the company proposes one individual as a director candidate, a shareholder may make a counter proposal to make another individual a director candidate during the meeting.

Further, a shareholder holding 1% or more of the voting rights (or holding 300 or more voting rights) may request the company add a certain agenda item for an upcoming shareholder meeting by making the request eight weeks prior to the scheduled date of the shareholder meeting.

### Resolution Requirement

The voting/quorum requirements for a shareholder meeting resolution differ depending on the agenda item to be resolved.

A super-majority vote, requiring two thirds or more of the affirmative votes among the shareholders present at the meeting, is required for some important matters such as amendments of the articles of incorporation, approval of mergers, dissolution of the company, and others. The quorum requirement, which is the attendance of shareholders holding more than half of all the

voting rights, may be relaxed by the articles of incorporation.

A simple majority vote, requiring more than half of the affirmative votes among the shareholders present at the meeting, applies to general matters such as the approval of financial statements, distribution of dividends, appointments of directors or statutory auditors, and others. The quorum requirement is the attendance of shareholders holding more than half of all the voting rights, which may be relaxed by the articles of incorporation.

There are some other resolution requirements for certain exceptional matters.

### Disclosure of Result of Resolution

In the case of a listed company, the voting results for each agenda item (ie, the number of affirmative votes, negative votes and abstentions) are required to be disclosed to the public.

## 5.4 Shareholder Claims

A shareholder has the right to request the company institute a suit against a director by itself seeking indemnification of the company by the director (or statutory auditors or an accounting auditor). If the company does not bring such a suit by itself within 60 days of the demand being made by the shareholder, the shareholder may, on behalf of the company, bring a suit (a derivative suit) against the director (or statutory auditors or an accounting auditor). In limited circumstances satisfying the requirements under the Companies Act, a shareholder may also bring a derivative suit against the directors (or statutory auditors or an accounting auditor) of a wholly owned subsidiary.

A shareholder may also file an action with the court to nullify certain corporate actions taken

by the company, such as the issuance of new shares, merger, company split and resolution of a shareholder meeting, if there exist grounds for such nullification.

## 5.5 Disclosure by Shareholders in Publicly Traded Companies

For publicly traded companies, a bulk shareholding report system exists. A shareholder holding more than 5% of the outstanding shares, as calculated pursuant to the relevant regulations, is required to file a bulk shareholding report within five business days of it satisfying such requirements. Thereafter, as long as the shareholder satisfies the requirements, the shareholder is required to file updated reports when material changes occur with respect to the information contained in the report, including the case of an increase or decrease of 1% or more in the shareholding ratio. In this regard, some beneficial owners satisfying the criteria stipulated in the FIEA are deemed to hold the relevant shares, but such regulation is not necessarily able to capture the ultimate beneficial owners.

In the case of institutional investors, some exceptions exist to relax the reporting timing and reduce the reporting contents.

The Council of Experts on the Stewardship Code, established by the Japanese Financial Services Agency, published *“Japan’s Stewardship Code”*. This Code is not a law or a legally binding regulation, but many institutional investors have accepted it and make disclosure in accordance with it. Under the Code, institutional investors should have a clear policy on voting and publicly disclose the same. Additionally, under the Code, institutional investors are expected to disclose voting records, including reasons for their voting decisions, for each investee company on an individual agenda item basis. In relation to dis-

closure/identification of beneficial owners of the shares held by institutional investors, amendment to the Stewardship Code and amendment to the Companies Act are now being discussed.

## 6. Corporate Reporting and Other Disclosures

### 6.1 Financial Reporting

The Companies Act provides for annual financial reporting requirements for all joint stock companies. Following the end of each fiscal year, a joint stock company is required to prepare:

- financial statements (consisting of a balance sheet, profit and loss statement, statement of changes in shareholders’ equity, and notes to financial statements);
- a business report; and
- supplementary statements to each of the foregoing.

When finalised, the financial statements and business report will ultimately be submitted to the company’s annual shareholder meeting for either approval or report to the shareholders.

Depending on the governance structure of the relevant joint stock company, the procedural requirements for finalising such documents will vary. In the case of a company with a board of directors, which is the most typical structure, its financial statements, business report and supplementary statements must be reviewed by the company’s statutory auditor or a board of statutory auditors (as applicable), and the financial statements and their supplementary statements must be reviewed and audited by the company’s accounting auditor (if applicable). The board of directors will then approve such documents, which will be approved by the shareholders, or

reported to the shareholders (in the case where the company's accounting auditor has issued an unqualified opinion as to the company's financial statements and other conditions are met), at annual shareholder meetings.

## Requirements Under the FIEA

Publicly traded companies (in this context, listed companies and other companies that are required to file annual securities reports under the FIEA) are required to prepare consolidated financial statements as well. In addition, under the FIEA, a publicly traded company is required to submit an annual securities report, which must contain audited financial statements (consolidated and non-consolidated) and be filed within three months of the fiscal year end. A publicly traded company is also required to submit a semi-annual report, which contains summary financial information and must be filed within 45 days of the semi-annual end. Financial information contained in semi-annual reports is required to undergo semi-annual review by the accounting auditor.

## Requirements Under the Stock Exchange

With a view to providing more timely financial information to public shareholders, the TSE Regulations also require that Japanese listed companies publish annual and quarterly summaries of consolidated financial results. Accounting auditors' review of financial information contained in such summaries is voluntary subject to certain exceptions. The Tokyo stock exchange requests that such summaries be made public within 45 days of the quarterly end.

## 6.2 Disclosure of Corporate Governance Arrangements

Corporate governance arrangements are generally required to be disclosed in business reports. Matters to be disclosed include:

- a summary of the company's corporate governance system, internal audit and statutory audit system, outside directors and statutory auditors and their relationships with the company; and
- details regarding compensation, corporate indemnification and D&O insurance.

Publicly traded companies also need to disclose in annual securities reports certain information regarding corporate governance.

In addition, the TSE Regulations require that each listed company submit a corporate governance report based on the Corporate Governance Code. In the corporate governance report, each listed company must explain, among other matters:

- its basic policy on matters included in the Corporate Governance Code established by the Tokyo stock exchange;
- the reasons for non-compliance with any of the principles of the Corporate Governance Code (if applicable);
- any disclosures required under the Corporate Governance Code;
- the composition of shareholders (eg, foreign shareholders, top ten largest shareholders, controlling shareholders, if any);
- the measures for protection of minority shareholders and group management policy where a listed company has a listed subsidiary, parent company, listed downstream affiliate, or upstream affiliate;
- its corporate governance system, including appointment of outside directors;
- the initiatives with respect to shareholders or other stakeholders; and
- its internal control system.



The Corporate Governance Code recommends that companies listed on the Prime Market provide English-language versions of key disclosure documents.

## 6.3 Companies Registry Filings

A joint stock company is required to file certain matters in a commercial registry, which is administered by the legal affairs bureau, upon incorporation and whenever any change to such matters arises. Matters required to be so registered include:

- corporate name, business purposes, amount of paid-in capital, the class and number of shares;
- the type and number of stock acquisition rights;
- directors, statutory auditors, accounting auditor, branch manager and other statutory organs;
- branches;
- merger, demerger and other statutory reorganisations; and
- dissolution and liquidation.

Matters registered in the commercial registry are publicly available, while the filings made to the legal affairs bureau are not. The legal affairs bureau is tasked with review of the application to confirm if the filings comply with the statutory requirements for the matters required to be registered and it may reject the application if the statutory requirements are not satisfied.

A failure to file a required commercial registry may result in a civil penalty not exceeding JPY1 million.

## 7. Audit, Risk and Internal Controls

### 7.1 Appointment of External Auditors

The following categories of joint stock companies must appoint an accounting auditor:

- a large-sized company (*daigaisha*);
- a company with an audit and supervisory committee; and
- a company with nominating and other committees.

An accounting auditor must be appointed from among external auditing firms or licensed accountants. For publicly traded companies, the accounting auditor usually provides audit certification on the financial statements filed under the FIEA.

In order to ensure independence of an accounting auditor, the Companies Act bars interested firms or persons with ties to the company from serving as an accounting auditor. Also, with the aim of shielding an accounting auditor from undue influence from the management, the board of statutory auditors (or their equivalent), rather than the board of directors, has the right to approve the appointment, removal and compensation of the accounting auditor.

With respect to an accounting audit for a listed company, a statutory registration system is in place where the Japanese Institute of Certified Public Accountants assesses the appropriateness of an external auditing firm, etc, that engages in an accounting audit.

### 7.2 Requirements for Directors Concerning Management Risk and Internal Controls

The Companies Act requires any large-sized company (*daigaisha*), any company with an audit



and supervisory committee and any company with nominating and other committees to determine and establish its internal control system to ensure that the company and its corporate group operate in a compliant and appropriate manner. In the case of a company with a board of directors, the board must decide the basic framework of the internal control system to be established. The establishment and implementation of an appropriate internal control system are generally considered to form part of the duties of due care of directors.

A joint stock company is required to outline the decisions made by the board of directors with respect to its internal control system and the implementation of the internal control system in its annual business report. The internal control system is audited by statutory auditors and the board of statutory auditors. Under the TSE Regulations, each listed company must describe its basic policy and implementation status of the internal control system in a corporate governance report as well.

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