

## RECENT MOVES IN JAPAN TOWARDS TOUGHER CORPORATE COMPLIANCE

"Japan Inc" is now back on the front pages with many Japanese corporations increasingly pursuing significant M&A opportunities internationally given the mature market at home and high levels of cash reserves.

The corporate landscape in Japan has also been changing in other ways in recent years. As a consequence of a number of high-profile corporate scandals, Japanese legislators have been busy revising legislation to further improve corporate governance in the world's third biggest economy.

This article focuses on three such reforms:

- the bolstering of the role of independent outside directors;
- the introduction of Japan's first ever plea-bargaining regime; and
- the release of Japan's "Principles for Listed Companies Dealing with Corporate Malfeasance".

For the reasons explained below, global companies with operations in Japan should keep in mind this shift towards more regulation.

### More robust independent directors

Until recently, Japan's reputation for overall sound corporate governance was subject to criticism as the statutory requirements in relation to outside directors did not require a sufficient degree of independence from company management and there was historically a very low number of independent outside directors on most Japanese boards. These concerns in part drove responsive changes to Japan's Companies Act and the introduction of Japan's "Corporate Governance Code".

In 2015, the Companies Act was amended to create new eligibility requirements for outside directors which increased their independence from company management.

Further, an additional rule in the Corporate Governance Code came into force in June 2015 effectively requiring listed companies to appoint at least two independent outside directors. Whilst this rule is not legally binding, listed companies who choose not to appoint such directors must publicly disclose their reasons.

### Key issues

- Japanese legislators have been working to improve corporate governance in Japan.
- Amendments to the Companies Act and a new Corporate Governance Code have led to a big increase in listed companies appointing independent outside directors.
- A new plea-bargaining regime will come into effect on 1 June 2018 creating a new compliance risk for corporations with operations in Japan.
- The Tokyo Stock Exchange's "Principles for Listed Companies Dealing with Corporate Malfeasance" sets out guidance that Japanese listed companies should follow when investigating suspected cases of corporate misconduct.

Despite initial inertia from many Tokyo boards which were long dominated by internally appointed directors, the rule has led to over 80% of businesses listed on the Tokyo Stock Exchange now having at least two or more independent outside directors, a dramatic increase from only around 30% of listed enterprises having any outside directors as recently as 2015.

Global companies with listed subsidiaries in Japan should be aware of the growing importance of independent outside directors.

### **Plea-bargaining system**

Japan's plea-bargaining regime will come into effect in June 2018, creating a new compliance risk for corporations with Japan operations.

Prosecutors may dismiss or reduce criminal charges or agree a punishment outcome if the individual or company provides evidence in relation to certain offences, including bribery and bid-rigging. In contrast to the US system, such evidence must relate to the alleged offences of *other* individuals or companies.

Thus, a person or company may potentially seek to reduce or avoid their own criminal guilt by giving false evidence in relation to innocent third parties, although there are safeguards in place to reduce this risk. These include the compulsory involvement of lawyers in the plea bargain negotiation process and sanctions for providing false or misleading evidence.

Global companies with a Japan presence should be aware of the potential risk. For example, a junior staff member terminated and prosecuted for criminal misconduct may seek to implicate an innocent manager to reduce or escape his/her own culpability.

This potential new risk underlines the importance of a well-structured, active and senior management-led compliance culture and effective whistleblower procedures.

### **Principles for Listed Companies Dealing with Corporate Malfeasance**

In 2016, the Japan Exchange Regulation authority (the "JPX") of the Tokyo Stock Exchange released its *"Principles for Listed Companies Dealing with Corporate Malfeasance"* which set out overarching guidance that Japanese listed companies should follow when investigating suspected cases of corporate misconduct.

Whilst the Principles are not legally binding on listed companies, the JPX has announced that it will consider the extent to which listed businesses have adopted the Principles when considering penalties or the potential delisting of corporations who are guilty of corporate wrongdoing.

The Principles encourage companies to establish a truly independent and expert third-party investigation committee with little or no oversight by or relationship with the company subject of the investigation.

The other main components of the Principles encourage companies to ascertain the fundamental, underlying cause of the malfeasance in question, promptly implement remedial measures and make prompt and appropriate information disclosures to the authorities and relevant stakeholders.

Global companies with a listed Japan presence may be well advised to consider the significance of the Principles in relation to not only their Japan operations but also potentially their businesses in other parts of the world.

## **Conclusion**

Global corporates with Japan operations should take particular note of the fact that many of the aforementioned corporate scandals came to light due to employee whistleblowing which, until only around ten years ago, was rare. A growing focus on compliance generally, more independent outside directors and less employee 'loyalty' to their employers due to increasing labour mobility and the shift from permanent to non-permanent forms of employment means that whistleblowing will probably increase in the future. This further underscores the importance of having properly structured and implemented compliance procedures on the ground in Japan.

## CONTACTS

### TOKYO

**Tatsuhiko Kamiyama**  
Partner

**T** +81 6632 6395  
**E** tatsuhiko.kamiyama  
@cliffordchance.com

**Masayuki Okamoto**  
Partner

**T** +81 6632 6665  
**E** masayuki.okamoto  
@cliffordchance.com

**Peter Coney**  
Counsel

**T** +81 3 6632 6646  
**E** peter.coney  
@cliffordchance.com

### ASIA PACIFIC

**Jenni Hill**  
Partner

**T** +61 8 9262 5582  
**E** jenni.hill  
@cliffordchance.com

**Nish Shetty**  
Partner

**T** +65 6410 2285  
**E** nish.shetty  
@cliffordchance.com

**Kabir Singh**  
Partner

**T** +65 6410 2273  
**E** kabir.singh  
@cliffordchance.com

**Wendy Wysong**  
Partner (Washington  
DC); Foreign Legal  
Consultant (Hong Kong)

**T** +852 2826 3460  
**T** +1 202 290 7634  
**E** wendy.wysong  
@cliffordchance.com

**Ali Burney**  
Counsel

**T** +65 6506 1964  
**E** ali.burney  
@cliffordchance.com

**Kate Godhard**  
Counsel

**T** +61 2 8922 8021  
**E** kate.godhard  
@cliffordchance.com

**Kirsten Scott**  
Counsel

**T** +61 8 9262 5517  
**E** kirsten.scott  
@cliffordchance.com

**Lei Shi**  
Consultant

**T** +852 2826 3547  
**E** lei.shi  
@cliffordchance.com

**Tess Forge**  
Foreign Registered  
Lawyer

**T** +852 2825 8888  
**E** tess.forge  
@cliffordchance.com

**Nicholas Turner**  
Foreign Registered  
Lawyer

**T** +852 2825 8854  
**E** nicholas.turner  
@cliffordchance.com

**Feifei Yu**  
Associate

**T** +852 2825 8091  
**E** feifei.yu  
@cliffordchance.com

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance (Gaikokuho Kyodo Jigyō)

Palace Building, 3rd floor

1-1, Marunouchi 1-chome, Chiyoda-ku, Tokyo  
100-0005, Japan

© Clifford Chance 2018

Abu Dhabi • Amsterdam • Barcelona • Beijing •  
Brussels • Bucharest • Casablanca • Dubai •  
Düsseldorf • Frankfurt • Hong Kong • Istanbul •  
London • Luxembourg • Madrid • Milan •  
Moscow • Munich • Newcastle • New York •  
Paris • Perth • Prague • Rome • São Paulo •  
Seoul • Shanghai • Singapore • Sydney •  
Tokyo • Warsaw • Washington, D.C.

Clifford Chance has a co-operation agreement  
with Abuhimed Alsheikh Alhagbani Law Firm  
in Riyadh.

Clifford Chance has a best friends relationship  
with Redcliffe Partners in Ukraine.