# A COMPARATIVE ANALYSIS: CORPORATE GOVERNANCE AND LABOR AND EMPLOYMENT RELATIONS IN JAPAN

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## I. INTRODUCTION

Mark Roe and Margaret Blair note, "In recent years legal and finance scholars who have studied the institutions of control and governance in larger corporations have focused on the relationship between shareholders and managers . . . But little energy has gone into analyzing the role of employees in such governance."[1] In Japan, by contrast, the role of employees is one of the most important themes in the corporate governance debate. Professor Kenjiro Egashira, a leading corporate law professor at Tokyo University, wrote: "There has been a consensus among most corporate law professors that, irrespective of the principles and theories stated in the corporate law, in practice larger companies are administered by prioritizing interests of employees including both blue and white collar workers."[2] This implies that, in spite of the principle that shareholders own a company and thus it should prioritize shareholder's interests, in practice, companies in Japan are administered for employees' interests. Another leading economist, Professor Mitsuhiro Fukao, stated that priority of access to the companies' assets is given in the following order: 1) creditors; 2) regular workers; 3) management; 4) shareholders; and, lastly, 5) non-regular workers.[3] Here again, regular

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1. EMPLOYEES AND CORPORATE GOVERNANCE 1 (Margaret Blair & Mark Roe eds., 1999).

2. Kenjiro Egashira, *Koporeto Gabanansu wo Ronzuru Igi (The Significance to Discuss Corporate Governance)*, *in* 1364 SHOJI HOMU 3 (1994).

3. Mitsuhiro Fukao, *Nihon no Kinyu Sisutemu Fuan to Koporeto Gabananse Kozo no Jakuten (Insecure Financial System and Weakness of Corporate Governance in Japan)*, *in*

workers have priority over shareholders and even over management. Professor Noriyuki Itami explains and justifies such employee-centered corporate governance by the fact that the contributions and risk exposure of the core employees are greater than those of shareholders, and that employees invest a hidden contribution via the seniority based wage and retirement allowance system.[4]

Regardless of whether one supports such employee-centered corporate governance or not, it cannot be denied that employment relations have been vitally important in the debate on Japanese corporate governance. This article attempts to clarify the several features of corporate governance in Japan viewed from a comparative perspective of employment and industrial relations. By analyzing and comparing the features of shareholders, management and employees in Japan with those in the United States and Germany, this article first suggests that Japanese corporate governance follows a stakeholder model as opposed to the Anglo-Saxon shareholder model. Second, however, an important difference exists between the German and Japanese stakeholder models: namely, that the Japanese stakeholder model significantly relies on customary practices and thus shows a striking contrast with the institutionalized German stakeholder model. Third, given drastic environmental changes surrounding Japanese corporations, this paper analyzes whether or not such a non-institutionalized Japanese corporate governance model will remain untouched.

## II. COMPARATIVE ANALYSIS OF CORPORATE GOVERNANCE AND LABOR RELATIONS IN JAPAN

### *A. Shareholders in Japan*

#### 1. Stable and Long-Term, Silent Shareholders

The distinctive feature of traditional corporate governance in Japan has been the existence of stable and long-term shareholders and widespread cross-shareholding (see Table 1).

**Table 1: Ratio of Stockholders in the United States, Japan and Germany**

MASAHIKO AOKI ET AL, SHIJO NO YAKUWARI, KOKKANO YAKUWARI (THE ROLE OF THE MARKET, THE ROLE OF THE STATE) 178 (1999).

4. HIROYUKI ITAMI, JINPON SHUGI KIGYO (EMPLOYEE-CENTERED CORPORATION) (1993); HIROYUKI ITAMI, NIHON-GATA KOPORETO GABANANSU (JAPANESE-STYLE CORPORATE GOVERNANCE) (2000).

(by presumed purpose of investment) (%)

***Source***: MICHAEL PORTER ET AL., CAPITAL CHOICES: CHANGING THE WAY AMERICA INVESTS IN INDUSTRY (1992).

Historically, in the immediate years after WWII, *Zaibatsu* or financial combines were dissolved, holding companies were prohibited by the Anti-Monopoly Law, and shareholding by corporations was generally prohibited. The percentage of individual shareholders was as high as 69.1% in 1949, and there were no stable long-term shareholders. However, the corporate shareholdings, namely shares held by financial institutions and by business corporations, increased steadily and by the mid-1960s surpassed shareholding by individuals. In 1990, corporate shareholding reached 70.4% and the percentage of individual shareholding stood at 23.1% (Figure 1).

**Figure 1: Distribution of Unit Shares Held by Types of Shareholders**

***Source***: The National Conference of Stock Exchanges, The 1999 Shareownership Survey (June 26, 2000).

In Japan, it is quite common for large business partners to own each other's stock (cross-shareholding). When such cross-shareholding evolves among banks from which other companies obtain long-term credit, these banks become "main banks" for those companies.[5] According to the Top Management Survey conducted by the Inagami group in 1999,[6] 98.4% of surveyed companies have "stable" shareholders. In the survey, the notion of stable shareholders was not defined. Therefore, the response relied on the respondents' notion of stability. Non-response was only 0.7% so more than 99% of

5. Ryuichi Yamakawa, *The Silence of Stockholders: Japanese Labor Law from the Viewpoint of Corporate Governance*, 38-11 JAPAN LAB. BULL. 5 (1999).

6. The survey to the top management on corporate governance (hereinafter "Top Management Survey") was conducted in February 1999, by a study group headed by Professor Takeshi Inagami, Tokyo University, in the Research Institute for Advancement of Living Standards (RIALS), a think tank of RENGO. The study group, to which the author belonged, distributed questionnaires to the top management in all 1,307 companies listed in the first section of the Tokyo Stock Exchange and received responses from 731 companies. The resultant analysis was published in GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN) 346 (Takeshi Inagami/RIALS eds., 2000).

respondents have an established notion of stable shareholders. The percentage of shares held by stable shareholders in all issued shares is 53.8%. Of surveyed companies, 39.2% have cross-shareholdings with stable shareholders.

Several factors contributed to the background of this structure of shareholding. Though *Zaibatsu* were dissolved by the order of the Occupation Authority, personal networks among *Zaibatsu* families caused a re-gathering of *Zaibatsu*-related companies. Relaxing of anti-monopoly regulations facilitated such trends. Japan's enrollment in the OECD in 1964—entailing liberalization of capital markets to foreign investment—induced Japanese corporations to develop a pattern of cross-shareholding to defend themselves against foreign acquisition.[7]

These stable shareholders are not typically motivated by short-term profit. Thus, shareholders of large Japanese companies tend to be "silent."[8] This allows Japanese companies to pursue long-term strategies and it has been evaluated positively. According to the Top Management Survey, 61.3% of respondents accept the current percentage of stable shareholders affirmatively and 12.9% of them want to increase stable shareholders. As for cross-shareholding, 52.5% of respondents accept the current situation and 4.7% of them want to increase it.[9]

### 2. Recent Developments

However, it should not be overlooked that 23.7% of top management think the percentage of stable shareholders should be reduced and 33.3% of them are negative towards cross-shareholdings.[10] A recent survey[11] reports that cross-shareholdings, especially those between banks and their customers, are now being dissolved in a rapid pace. Such trends of unwinding cross-shareholdings started in 1996, and the cross-shareholding ratio (value-

7. Kunio Ito, *Kabushiki Mochiai (Cross-Shareholding)*, *in* 1 NIHON NO KIGYO SHISUTEMU: KIGYO TO HA NANIKA (CORPORATION SYSTEM IN JAPAN: WHAT IS CORPORATION?) 154 (Hiroyuki Itami et al. eds., 1993).

8. Yamakawa, *supra* note 5; JONATHAN CHARKHAM, KEEPING GOOD COMPANY: A STUDY OF CORPORATE GOVERNANCE IN FIVE COUNTRIES 81 (1994).

9. *See supra* note 6, at 330-331.

10. *Id*.

11. Nissei Kiso Kenkyujo (NLI Research Institution), *1999 Kabushiki Mochiai Jokyo Chosa (The Fiscal Year 1999 Cross-Shareholding Survey)*, *available at* http://www.nli-research.co.jp/index-j.html; *see also* Fukao, *supra* note 3, at 157.

based) declined from 16.94% in 1995 to 10.53% in 1999 (see Table 2).[12]

**Table 2: Cross-Holding Ratios by Shareholder (Value-Based, %)**

Another important development in structure of shareholders is the rapid increase of foreign investors. The ratio of shares owned by foreigners rose from 4.2% in 1990 to 12.4% in 1999, on a unit share basis and 4.7% in 1990 to 18.6% in 1999, on a market value basis (see Figure 1 and Figure 2).

**Figure 2: Distribution of Shares by Types of Shareholders (value based)**

***Source***: The National Conference of Stock Exchanges, The 1999 Shareownership Survey (June 26, 2000).

Therefore, the majority of management still recognizes the merits of stable and cross-shareholding. However, there has been a decline in stable cross-shareholding and an increase in foreign investment. The latter phenomenon will require more shareholder value-oriented corporate governance than ever. Therefore, the development of the emerging changes in Japan's shareholding structure and their impact on corporate governance should be closely observed (see 3).

### *B. Board of Directors and Auditors*

#### 1. Overview of Corporate Management System

Japanese corporate law is influenced by German law and, subsequently, by United States' law.[13] As a result, the legal structure of Japanese corporate management and the corporate monitoring system show some unique features.

The Japanese Commercial Code, enacted in 1899, adopted a dual monitoring structure of managing directors and auditors modeled on the German law. In 1950, Japanese corporate law introduced a system

12. When cross-holdings began declining from the fiscal year 1996, business companies first began selling bank stocks, followed by banks selling business company stocks. However, the 1999 survey results show that both banks and business companies are actively unwinding cross-holdings in each other. Hideaki Inoue, *Companies Continue to Unwind Cross-Shareholdings—The Fiscal 1999 Cross-Shareholding Survey*, NLI RESEARCH No. 145, *available at* http://www.nli-research.co.jp/eng/index-e.html.

13. *See generally* HIROSHI ODA, JAPANESE LAW 216 (2nd ed. 1999).

of a "board of directors" due to the influence of U.S. law. Under this system, the board of directors supervises the corporate administration through a representative director and other directors. However, since the auditor system was never abolished, corporate administration is supervised by both the board of directors and auditors (Figure 3).[14]

**Figure 3: Corporate Management System**

2. Board of Directors

In the Japanese corporate management system, the board of directors and, especially, the representative directors have real power to govern the corporation. From a comparative perspective, the first dominant feature of the board of directors is its size: Boards with more than twenty members were common in Japan.[15] Excessive size has been cited as a key cause of board dysfunction. In the late 1990s, many companies introduced the executive officer system in order to reduce the number of directors. According to the Top Management Survey, 48.6% of surveyed companies had already reduced the size of the board by 1999. Nonetheless, the average number of directors is 17.5,[16] which is still much larger than in the United States (12).[17]

The second feature of the board of directors is that the board members are similar or analogous to employees in terms of mentality, function and remuneration. In terms of mentality, according to the Top Management Survey, 75.6% of board members are promoted from within a company, not hired from the outside.[18] Most of those remaining board members who are not promoted from within are from parent or affiliated companies. Therefore, the board members are not "outsiders" to the company. This internal promotion practice stems from democratization measures for Japan's economy, which were encouraged by the Occupation Authority after WWII. In 1947-48, pre-war and wartime management were purged and a young elite was promoted to management positions from within.[19] In accordance

14. Hiroyuki Kansaku, *Kororeto Gabanansu-ron to Kaisha-ho (Debate on Corporate Governance and Corporate Law)*, *in* GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN), *supra* note 6, at 169.

15. Noboru Kawahama, *Torishimariyaku-kai no Kantoku Kino (Supervisory Function of a Board of Directors)*, *in* KIGHO NO KENZEN-SEI KAKUHO TO TORISHIMARIYAKU NO SEKININ 38 (Shigeru Morimoro et al. eds., 1997).

16. *See supra* note 6, at 337 (Q19-8).

17. See CHARKHAM, *supra* note 8, at 188.

18. *See supra* note 6, at 324.

19. Tetsuji Okazaki, *Senji Keikaku Keizai to Kigyo*, *in* 4 GENDAI NIHON SHAKAI: REKISHITEKI ZENTEI 103, 114, 125 (Tokyo Daigaku Shakai Kagaku Kenkyujo ed., 1993).

with the spread of long-term or lifetime employment policies, the promotion of incumbent employees to board memberships is commonplace. The board membership is given to employees as a final stage of promotion for their excellent performance throughout their working career and it denotes the crowning success of their career as an employee. This is one of the main reasons for the large size of the typical Japanese board.

With regard to remuneration, there is no significant gap between the remuneration of board members and that of employees. As Figure 4 shows, there is apparent continuity of the remuneration profile between a department head (managerial employee) and an ordinary (junior) director. As a result, the remuneration gap between employees and board members is quite narrow. For instance, the averaged annual remuneration of board members amounts to only nine times that of new entrants graduated from universities.

**Figure 4: Employee and Management Career and Remuneration in Japanese Corporations**

***Source***: Top Management Survey: Interim Report, 127 RENGO SOKEN REPORT DIO 19 (1999).

In terms of functions, ordinary (junior) directors usually have a double role as both junior board members and managerial employees of their respective departments. According to the Top Management Survey analysis, half of all board members fit into this functional category.[20] According to another survey,[21] 73.3% of the annual salary of these "directors with employee function" is remuneration for the employee function and 26.7% is for the director function. Therefore, junior directors with this double function are more like employees than directors. In a sense, Japanese management boards have accepted employee representatives by accepting these "directors with employee function."

These attributes of board members significantly influence Japan's stakeholder model of corporate governance. According to the Top Management Survey, only 8.5% of respondents support an opinion

20. According to Michio Nitta's analysis, the average number of board members is 17.5 and the average number of directors with employee functions is 8.3. Michio Nitta, *Nihon Kigyo no Koporeto Gabanansu: Genjo to Tenbo (Japanese Corporation and Corporate Governance: Present State and Future)*, *in* GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN), *supra* note 6, at 87.

21. *Romu Gyosei Kenkyu-jo, Saishin Yakuin Hoshu-Shoyo, Irokin no Jittai (Current State of Executives' Remuneration, Bonus and Severance Pay)*, 3395 ROSEI JIHO 2 (1999).

that "a corporation is the property of shareholders, and employees are merely one of the factors of production," whereas 85.8% support an opinion that "shareholders are not the only stakeholders of the corporation. Therefore, the interests of various stakeholders must be reflected in the corporate management."[22]

These features of the board of directors certainly facilitate cooperative labor and management relations and thus enhance the efficiency of corporate administration as seen below. However, the current board of directors system has been less effective in preventing illegal action or making itself accountable to shareholders. In practice, the nomination of vice-presidents and other executives is strongly influenced by the president's opinion.[23] Nearly half of all board members are "directors with employee function" and are thus subject to their employer's directions. As a result, the board of directors tends to be subject to the leadership of the representative director or president rather than vice versa.

### 3. Auditors

Auditors monitor the legality of a corporation's finance and directors' business administration.[24] Though this dual structure of management originates from German law, there are quite significant differences between the German supervisory board (*Aufsichtsrat*) and the Japanese auditor system.

First, whereas a German supervisory board at companies with more than 500 employees[25] consists of representatives of shareholders and those of employees, the Japanese auditor system is not a worker-participation scheme. The representative directors, who have a right to propose a list of nominees to a general shareholder meeting, de facto determine the appointment of Japanese auditors. It is rather common that the representative directors nominate auditors from

22. GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN), *supra* note 6, at 334. However, it is also noteworthy that 49.9% of respondents support the following opinion: "The primary role of the management is to enhance capital efficiency to maximize the profit of shareholders." Management becomes more conscious of capital efficiency than ever before. *Id.*

23. According to the Top Management Survey, 85.8% of respondents affirmed this statement. GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN), *supra* note 6, at 327.

24. In the smaller corporations (with capital of 100 million yen or less and debt is less than 10 billion yen), an auditor's power is confined to financial auditing and does not include scrutiny of business administration.

25. Companies with less than 500 employees are not obliged to establish an employee participated supervisory board. Currently, two-thirds of the German workforce is employed at such co-determination free companies. MANFRED LÖWISCH, ARBEITSRECHT (4th ed. 1996).

among the employees or board members.[26] Second, while the German supervisory boards have the power not only to audit finance and monitor business administration, but also to appoint and discharge board members, Japanese auditors do not have the latter power. As for the former jurisdiction over the financial and business administration, their scrutiny is narrowly understood to be confined to legality checks and does not extend to appropriateness.[27]

Because it is difficult to expect the board of directors to supervise the representative director's business administration, all efforts to reform the monitoring system in Japanese corporate law have concentrated on measures to strengthen the power of auditors and ensure their independence. In 1974, auditors' supervisory power was expanded to corporate administration. The 1981 amendment required an appointment of three or more auditors and at least one full-time auditor to larger companies. In 1993, the terms of auditors were expanded from two to three years (Art. 273, Para. 1, the Commercial Code). To strengthen their independence, outside auditors and auditor committee systems were required to larger companies.[28]

In spite of these amendments to strengthen the power and independence of auditors, it is said that the auditor system falls short of expectations.[29] Recently, the Corporate Governance Forum in Japan proposed a more radical reform plan: to allow parties to abolish the auditor system by adopting an American-style "board of directors" system utilizing non-executive directors.[30] Surprisingly, the interim draft of the revision of the Commercial Code[31] by the Legislative Council of the Ministry of Justice, an advisory council to the Minister of Justice, adopted the proposal (see 3).

26. Hideaki Kubori, *Nihon no Kaisha Soshiki no Jittai to Kororeto Gabanansu (The Reality of Japanese Corporation and Corporate Governance)*, 1050 JURISUTO 41 (1994).

27. While the debate over whether auditors' scrutiny covers the issue of efficiency or appropriateness of corporate administration continues, the majority opinion is that auditors' scrutiny is confined to legality check and it is the board of directors that supervises the issue of efficiency or appropriateness of corporate administration. *See* HITOSHI MAEDA, KAISHA HO NYUMON (PRIMER ON CORPORATE LAW) 238 (7th ed. 2000); KAZUSHI YOSHIHARA ET AL., 1 KAISHA HO (CORPORATE LAW) 192 (2nd rev. ed. 2001).

28. Art. 2 defines large companies as those that have capital exceeding 500 million yen or debts exceeding 20 billion yen (Special Measures Law to the Commercial Code on Audit).

29. KEIZAIDOYUKAI, 12 KIGYO HAKUSHO (WHITE PAPER ON CORPORATION) 7 (1996); YOSHIHARA, ET AL., *supra* note 27, at 185.

30. Corporate Governance Forum of Japan, *Corporate Governance Principles*, 212 BESSATSU SHOJI HOMU 43 (1998).

31. The interim draft was issued on April 18, 2001, *available at* http://www.moj.go.jp.

### *C. Employment*

Job security has a high priority in Japanese corporate governance. Employees in Japanese companies are not merely seen as a factor of production that can be adjusted in accordance with fluctuating economic needs. Instead, corporations treat employees as important constituents. This is attained by the employment security provided by labor law. From a comparative perspective, employment security regulations in Japan show several features.

#### 1. Caselaw Protection

The first feature is that employment security is provided for not by legislation, but rather by caselaw.[32] In European countries, labor legislation requires just cause for dismissals. However, in Japan, there is no such statute.[33] It is caselaw or judge-made law that provides these restrictions. Japanese courts established a rule called the "abuse of the right to dismiss" theory, which regards a dismissal without just cause as an abuse of the right to dismiss and thus null and void.

The "abuse of the right to dismiss" theory arose in the context of post-war socio-economic conditions that made protection of workers' employment security imperative. Immediately following Japan's defeat in World War II, when there was a shortage of food, a lack of employment opportunities and a superfluous workforce, dismissal meant loss of livelihood for many workers. Even after Japan overcame such difficult times and the long-term employment practice had become firmly established, dismissal was viewed as detrimental to a worker's seniority (a decisive factor in the personnel management and wage systems), for the seniority gained through previous employment does not necessarily carry over to new employment. Dismissal also placed such a worker at a serious disadvantage because

32. For details of dismissal law in Japan, *see* Yasuo Suwa, *Flexibility and Security in Employment: The Japanese Case*, 6 INT'L J. OF COMP. LAB. L. & INDUS. REL. 229 (1990); KAZUO SUGENO, JAPANESE LABOR LAW 395 (translated by Leo Kanowitz, 1992); Tadashi Hanami, *Japan*, *in* EMPLOYMENT SECURITY 187 (Roger Blanpain & Tadashi Hamami eds., 1994); Kazuo Sugeno & Yasuo Suwa, *The Internal Labour Market and its Legal Adjustments*, Paper No. 4, JAPAN INTERNATIONAL LABOR LAW FORUM (1995); Takashi Araki, *Re-examination of Employment Security in Japan in Light of Socio-economic Structural Changes*, *in* RODO KANKEI HO NO KOKUSAITEKI CHORYU (INTERNATIONAL TRENDS IN LABOR RELATIONS LAW) 193 (Koichiro Yamaguchi et al. eds., 2000).

33. The Labor Standards Law and other statutes prohibit discriminatory dismissals, dismissals of pregnant workers and dismissals of victims of work-related injuries. Unlike the American "at will" doctrine, the Labor Standards Law generally requires 30 days advance notice or an advance notice allowance in lieu of the notice (LSL, Art. 20). However, apart from these regulations, Japanese legislation does not require just cause for dismissals.

finding comparable employment was extremely difficult in Japan's external labor market.

Under such circumstances, Japanese courts thought that workers should be provided a degree of protection by restricting the employer's right to dismiss at will. Relying on the general clause of the Civil Code that prohibits abuse of rights (Civil Code Art. 1, Para. 3), Japanese courts handed down decision after decision holding that an objectively unreasonable or socially unacceptable dismissal was an abuse of the right to dismiss. Such dismissals were declared null and void. The theory of abuse of the right to dismiss was thus created by judicial precedent in lower courts and finally endorsed by the Supreme Court in 1975.[34]

Under this caselaw, an employer is required to demonstrate the existence of just cause. Courts interpret just cause very strictly and tend to deny the validity of the dismissal unless there has been serious misconduct by the worker. A court considers all of the facts favorable to a worker's case and strictly scrutinizes the reasonableness of the dismissal.

The remedies against unjust dismissals are highly protective. In many countries, unjust dismissals result in the payment of money in the form of damages or redundancy payment. By contrast, under the abuse of the right to dismiss theory in Japan, the employer is obliged not only to pay wages during the period of dismissal, but also to reinstate the dismissed employee because the dismissal is null and void.

As a result, if a dismissal is held to be abusive, the employer cannot dissolve the employment relationship with the employee no matter how much the employer pays the employee. Though payment of lost wages itself is a heavy burden for the employer,[35] on top of this, the employer must reinstate the worker. This functions as a disincentive for Japanese employers to resort to arbitrary dismissals.

### 2. Restraints on Economic Dismissals

The second feature of employment security regulation is that Japanese caselaw sets stringent restrictions on economic dismissals. Individual dismissals are universally restricted in most developed

34. *Nihon Shokuen Co.* 29 MINSHU 456 (Supreme Court, April 25, 1975).

35. Since there is no cap on the payment for lost wages, when a worker has spent 10 years to win the case, the employer is obliged to pay wages for the ten years, although the worker's intermediary incomes can be deducted up to 40% of the wages. *Beigun Yamada Butai*, 16 MINSHU 1656 (Supreme Court, July 20, 1962).

countries. However, regulations on economic dismissals vary from country to country. One of the features of Japanese caselaw is that it restricts economic dismissals more severely than in other developed countries.

The recession triggered by the oil crises in the 1970s caused Japanese companies to streamline and execute large-scale restructuring of their operations. However, since the long-term employment practice took root in Japanese corporate society by that time, major companies refrained from resorting to employment adjustment through dismissals. After careful consultation with their enterprise-based unions, corporate management chose to take various cost-cutting measures to avoid layoffs as much as possible. Such unions also cooperated with management in implementing relocation and transfer programs designed to avoid employment adjustment dismissals. The courts adopted the practices between larger companies and their unions as general rules concerning economic dismissals. As a result, caselaw dictates that any adjustment dismissal should be rejected as an abuse of the right to dismiss unless it meets four requirements.

First, there must be business-based need to resort to reduction of personnel. Second, the employer must take every possible measure to avoid adjustment dismissals, such as: reduction in overtime; reduction in regular hiring or mid-term recruitment; implementation of transfers (*haiten*) or "farming out" (*shukko*) with respect to redundant workers; non-renewal of fixed-term contracts or contracts of part-timers; and, solicitation of voluntary retirement. In other words, dismissals must be the last resort to cope with the economic difficulties. Third, the selection of those workers to be dismissed must be made on an objective and reasonable basis. Lastly, the management is required to explain the necessity of the dismissal, its timing, scale and method to the labor union or worker group if no union exists, and consult with them concerning the dismissals in good faith.

Among these four requirements, the second requirement (the "last resort" requirement) compels Japanese companies to exhaust all options to avoid economic dismissals. In Japanese employment relations, employers have many alternatives for cost reduction and maintaining redundant workers, so it is difficult for them to satisfy this requirement. At the least, the caselaw requires time-consuming process.

### 3. Relaxation of Economic Dismissals?

Recently, there is a noteworthy development concerning economic dismissals. Traditionally, as mentioned above, the validity of economic dismissals was determined by whether all four requirements are met or not. If one of four requirements was not satisfied, the dismissal was regarded as an abuse of the right to dismiss.

The recent Tokyo District Court decision[36] rejected this interpretation because it stated that there is no solid legal ground for insisting that all four requirements must be satisfied for economic dismissals. According to the Tokyo District Court, what the Court should determine is whether a dismissal is abusive or not. The so-called "four requirements" are nothing but "four factors" to analyze abusiveness. Therefore, according to the position of the Tokyo District Court, if one of the "four factors" (for example, consultation) is not met, such an economic dismissal can be held legal and valid by taking all other factors surrounding the dismissals into consideration.

It is too early to judge whether the new ruling by the Tokyo District Court will replace the current established "four requirements" rule because other district courts still support the traditional rule. However, at least it is worth mentioning that a new interpretation that facilitates economic dismissals is emerging. Having stated that, from a comparative view, even if the "four requirements" rule becomes the "four factor" rule, restrictions nevertheless will still be more stringent than in the United States[37] and probably more so than in Germany.[38]

36. *National Westminster Bank* (3rd Provisional Disposition), 782 RODO HANREI 23 (Tokyo Dist. Ct., Jan. 21, 2000).

37. In the United States, the classic employment at will doctrine is certainly eroding and is being modified by caselaw. Stringent anti-discrimination laws also restrain U.S. employers from arbitrarily dismissing employees. However, compared to situations in European countries and Japan, U.S. employers still enjoy more freedom to dismiss employees and restriction on economic dismissals hardly exists. *See* Clyde Summers, *Worker Dislocation: Who Bears the Burden? A Comparative Study of Social Values in Five Countries*, 70 NOTRE DAME L. REV. 1033, 1036 (1995).

38. Though German law requires detailed procedures for economic dismissals, including establishing a "social plan," if employers follow the procedures, it seems easier to reduce redundant employees in Germany than in Japan. Some point out that, in practice, economic dismissals are widely done in exchange for paying money. *E.g.* Oppolzer, *Individuelle Freiheit und Kollective Sicherheit im Arbeitsrecht*, ARBEIT UND RECHT 47 (1998); Neef, *Das Kündigungsschutzrecht zur Jahrtausendwende*, NEUE ZEITSCHRIFT FÜR ARBEITSRECHT 8 (2000).

### *D. Industrial Relations, Employee Participation and Corporate Governance*

The prominent feature of Japan's industrial relations is stable and cooperative relations between labor and management developed under enterprise unionism. Previously, some attributed Japan's cooperative labor relations to cultural factors, such as the Japanese people's "harmonious" and "non-strife prone" nature. However, from the end of World War II through the 1960s, Japan experienced turbulent labor management confrontations.[39] It is a rather recent phenomenon (after the first oil crisis) that industrial relations have become stable (see Figure 5). Therefore the cultural explanation is not persuasive.

**Figure 5: Dispute Acts and Workdays Lost**

Japan's current stable industrial relations are the result of the influence of the following three factors: 1) Japan's enterprise unionism, 2) wide-spread joint labor-management consultation practices, and 3) internal management promotion practices.

#### 1. Enterprise Unionism

Enterprise unionism[40] is a hallmark of Japanese industrial relations. Currently, 95.6% of unions in Japan are enterprise-based unions and 91.2% of all unionized workers belong to enterprise unions.[41] Enterprise unionism is a system in which unions are established within an individual enterprise, collectively bargain with a single employer and conclude collective agreements at the enterprise level. Enterprise unions within the same industry often join an industrial federation of unions and the industrial federations are affiliated with national confederations. However, industry-level collective bargaining is very rare.

39. *See* Kazuo Sugeno & Yasuo Suwa, *Introduction to Japanese Industrial Relations: A Legal Perspective*, JAPAN INT'L LABOR LAW FORUM, Paper No. 1 (1994); Takashi Araki, *Japan*, 34 BULL. OF COMP. LAB. REL. 49 (1999); KAZUTOSHI KOSHIRO, A FIFTY YEARS HISTORY OF INDUSTRY AND LABOR IN POSTWAR JAPAN, 6 JAPANESE ECONOMY & LABOR SERIES (2000). Nobuhiro Hiwatari states, "Japan's enterprise unionism emerged in the years after World War II, largely as an unintended outgrowth of revolutionary unionism . . . ." Nobuhiro Hiwatari, *Employment Practices and Enterprise Unionism in Japan*, *in* EMPLOYEES AND CORPORATE GOVERNANCE 276 (Margaret Blair & Mark Roe eds., 1999).

40. *See generally* Kazuo Sugeno & Yasuo Suwa, *The Three Faces of Enterprise Unions: The Status of Unions in Contemporary Japan*, JAPAN INT'L LABOR LAW FORUM, Paper No. 6 (1996).

41. Rodosho, *1997 Rodo Kumiai Kiso Chosa (Basic Survey on Labor Unions)* (1997).

An enterprise union organizes workers in the same company irrespective of their jobs. As a result, both blue and white-collar workers are organized in the same union. Enterprise unions normally confine their membership to regular workers, although there are no legal obstacles that prevent enterprise unions from organizing part-time workers or temporary workers.

There are several reasons for the dominance of this pattern of union organization.[42] Historically, Japan had little experience with industry-wide unionism before WWII, and the experience of the wartime regime that mobilized all workers into units at the enterprise level may have had some influence. After the war, when employers could no longer suppress union activities, workers freely used the enterprise-level workplace approach as the most convenient basis for organization.

Enterprise unionism continues to predominate, however, because it serves well as a key component of Japanese employment relations. Under the long-term employment system, dismissals are avoided at all cost. In exchange, workers accept the flexible adjustment of working conditions.[43] In the highly developed internal labor market, employees are transferred within a company and receive in-house education and on-the-job training. The promotion and wages of each employee are decided mainly by that individual's length of service and performance. In this context, industrial-level or national-level negotiations make little sense. Enterprise unions and enterprise-level collective bargaining have been the most efficient mechanism in reconciling the requirements of an internal labor market with the workers' demands. When unions have their basis in a particular company, they tend to be more pragmatic than ideological and more conscious about their own company's productivity and competitiveness.

42. Araki, *supra* note 39, at 54.

43. The above-mentioned caselaw that restricts economic dismissals implies a lack of numerical or external flexibility in employment relations. In order to compensate for such rigidity, caselaw has introduced functional or internal flexibility. Japanese courts held that Japanese employers are allowed to order transfers of employees based upon business necessity and to adjust terms and conditions of employment by "reasonable" modification of work rules. *See* Takashi Araki, *Accommodating Terms and Conditions of Employment to Changing Circumstances: A Comparative Analysis of Quantitative and Qualitative Flexibility in the United States, Germany and Japan, in* LABOUR LAW AND INDUSTRIAL RELATIONS AT THE TURN OF THE CENTURY 509 (Chris Engels & Manfred Weiss eds., 1998).

### 2. Joint Labor-Management Consultation

Joint labor-management consultation is an established practice in Japanese industrial relations. Currently, 41.8%[44] of all surveyed establishments have such consultation bodies.[45] In unionized establishments, the figure is greater at 84.8%. In many countries, labor-management consultation was not voluntarily established. Therefore, the state intervened and forced companies to establish works councils or other channels for communicating and informing employees. In Japan, by contrast, labor-management consultation was voluntarily established without any legal intervention. This consultation is also strongly related to the historical development of Japan's industrial relations.[46] After WWII, Japan experienced harsh confrontations between labor and management. Both parties were exhausted by adversarial relations and looked for new, more pragmatic and cooperative relations.

In 1955, business circles under the auspices of the Ministry of International Trade and Industry (MITI) and the American government, to promote the Productivity Increase Movement and joint consultation practices, established the Japan Productivity Center. Though leftist unions, especially SOHYO, were skeptical and regarded the Movement as a new type of rationalization or exploitation and strongly opposed it, the national confederation of moderate unions (SODOMEI) participated in the Movement on the condition that the opinions of the union concerned should be fully respected. Thus, SODOMEI and the Japan Productivity Center confirmed the three following basic principles of the Productivity Increase Movement:

> 1) The productivity increase shall enhance employment security. Redundancies in transitional stages shall be resolved not by layoffs, but by transfers or other measures.
>
> 2) Labor-management consultation must be promoted to determine concrete measures to increase productivity.
>
> 3) The fruits of increased productivity must be distributed fairly among management, employees and customers in accordance with the conditions in the national economy.

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44. The figure is smaller than that in the previous survey in 1994 (55.7%). This is largely attributable to the difference in the size of surveyed establishments. The 1994 survey sampled establishments with more than fifty employees and the 1999 survey sampled those with more than thirty.

45. Japan Ministry of Labor, *Survey of Communication Between Labor and Management in 1999*, *available at* http://www.jil.go.jp/kisya/daijin/20000619_02_d/20000619_02_d.html.

46. Araki, *supra* note 39.

In short, Japanese employers promised not to lay off redundant employees as a result of increased productivity and to maintain their employment by transfer and re-training. At the same time, to enhance mutual understanding and smooth implementation of productivity enhancement, they advocated establishing joint labor-management consultation. These three basic principles, namely employment security, dense communication through joint consultation and fair distribution of the enhanced productivity, became the basic principles of the Japan's cooperative labor relations in the subsequent years.

Left-wing unions remained skeptical of the productivity increase movement. However, after the defeat of the leftist union movement during the giant confrontation that resulted from the *Miike* coal mine dispute in 1960, pragmatic and cooperative labor relations gradually took root in Japanese industrial relations. Labor and management voluntarily established consultation mechanisms and developed rich communication through joint consultation. Employers provided various information for unions and unions cooperated with management in increasing productivity. In fact, this information flow was indispensable in acquiring the unions' cooperation for implementing restructuring plans entailing wide-range transfers to avoid economic dismissals. Japanese labor and management learned from their bitter confrontations that adversarial relations benefited neither party and found that by establishing cooperative relations and enhancing productivity, they could change a zero-sum game into a win-win game.

However, it should not be overlooked that joint consultation was encouraged by the sanction of a union's right to bargain. In accordance with the stabilization of Japan's industrial relations, some point out the formalization of joint consultation (3.3).

### 3. Internal Promotion of Board Members

Internal promotion of management also contributed to Japan's cooperative industrial relations and employee-centered corporate governance. In larger companies in Japan, union shop agreements are fixed. Under the union shop agreement, all employees must join the union. This means that current executives were members of the enterprise union in their 20's or 30's when they were rank-and-file

white-collar workers.[47] Furthermore, according to the Top Management Survey, 28.2% of top management was not only union members, but also leaders of an enterprise union.[48] In a sense, labor-management relations in Japanese enterprises are the relation between present union members and former union members (sometimes between current union leaders and former union leaders). This brings about a consciousness that both labor and management belong to the same community, facilitates labor and management to find common interests and leads Japanese management to take a consensual—rather than an adversarial—approach.[49]

Currently, nearly half of board members are directors-with-employee-function. By accepting directors-with-employee-function, it can be said that Japanese corporations established a channel to voice employees' opinions to corporate management. As discussed later, government is now planning to drastically modify the structure of management system. It will significantly affect the internal promotion system and the acceptance of directors-with-employee-function practice.

### *E. Non-Institutionalized Stakeholder Model Corporate Governance*

First, it should be reconfirmed that Japanese corporate governance has shown typical features of the stakeholder model as far as employment relations are concerned. Unlike the classic shareholder-value maximizing model, employees are not treated as an adjustable resource for corporate administration. Employment security is highly respected. Employees' voices are reflected and respected in corporate governance through internal promotion of board members, including directors-with-employee-function and through joint labor-management consultation.

Second, from the viewpoint of legal intervention concerning corporate governance and labor relations, both the German stakeholder model and the American shareholder model are regulated and required by legal intervention. By contrast, the Japanese stakeholder model heavily relies on customary practices. In

47. As Japanese enterprise unions organize workers in the same company irrespective of their position, both blue- and white-collar workers are organized in the same union.

48. GENDAI NIHON NO KOPORETO GABANANSU (CORPORATE GOVERNANCE IN CONTEMPORARY JAPAN), *supra* note 6, at 339.

49. Takashi Araki, *The Japanese Model of Employee Representational Participation*, 15 COMP. LAB. L.J. 143, 153 (1994).

Germany, the Civil Code requires a long period of notice[50] for dismissals, socially justifiable reasons are required by a statute (Kündigungschutzgesetz vom 25.8.1969) and dismissal procedures are also heavily regulated requiring works councils' involvement. Through these legal regulations, a classic concept of freedom of dismissal is explicitly modified. As for worker participation, two types of co-determination, namely co-determination at the level of the supervisory board (*Aufsichtsrat*),[51] and co-determination between employer and works council (*Betriebsrat*) at establishment level[52] are required by respective laws. In particular, co-determination rights of works councils[53] strongly affect the German system of corporate governance. In order to take action concerning co-determination matters prescribed by the Works Constitution Act, an employer must obtain the consent of the works council. An employer's unilateral action is generally understood to be null and void. When an employer and a works council cannot reach an agreement on co-determination matters, the case is referred to an arbitration committee (*Einigungsstelle*).[54] The decision made by the arbitration committee is regarded as the agreement between the employer and the works council and becomes binding for both sides. Therefore, the German stakeholder model is a legally institutionalized model.[55]

50. A notice period ranges from 4 weeks to 7 months, depending on the length of service (Art. 622, Para. 1 and 2, Civil Code).

51. Co-determination at the supervisory board is regulated by the 1951 Coal and Mine Co-determination Act (Montan-Mitbestimmungsgesetz vom 21.5.1951), which applies to coal and mine companies with more than 1,000 employees; the 1952 Works Constitution Act (Betriebsverfassungsgesetz vom 11.10.1952), which applies to companies with 500 or more employees; and, the 1976 Co-determination Act (Mitbestimmungsgesetz vom 4.5.1976), which applies to companies with more than 2,000 employees. *See* HROMADKA & MASCHMANN, 2 ARBEITSRECHT 197 (1999); ZÖLLNER & LORITZ, ARBEITSRECHT 604 (1998); MANFRED WEISS, LABOUR LAW AND INDUSTRIAL RELATIONS IN GERMANY 190 (1995).

52. Co-determination between the employer and works council is comprehensively regulated by the 1972 Works Constitution Act (Betriebsverfassungsgesetz).

53. Though the co-determination right covers various matters, the most important is the social matters enumerated in Art. 87 of the Work Constitution Act, e.g. the order within the establishment, the beginning and end of the daily working hours, the distribution of working hours over the days of the week, temporary reduction or extension of normal working hours, time, place and mode for payment, etc. As for economic matters, a works council in an establishment with twenty or more employees has a co-determination right over a so-called social plan or a compensation agreement to be given to employees affected by a restructuring of the establishment (Art. 112, Work Constitution Act). *See* WEISS, *supra* note 51, at 181.

54. An arbitration committee is a tripartite body comprised of an employer-designated member, a works council-designated member and a chairman appointed by both sides.

55. According to the Report of the Commission on Codetermination, which re-examined the merits and demerits of current co-determination system, these institutionalized co-determination systems are evaluated affirmatively. *1998 Bericht der Kommission Mitbestimmung, Mitbestimmung und neue Unternehmenskulturen—Bilanz und Perspektiven* (1998), *available at* http://www.mpi-fg-koeln.mpg.de/bericht/endbericht/.

Even the American shareholder-value model is, in a sense, established and sustained by legal intervention. Since the 1970s, American employers endeavored to introduce employee participation schemes to enhance productivity and quality of work life. However, American law, as interpreted by the National Labor Relations Board and Federal courts, prohibits most such employee involvement as illegal intervention into "labor organization" on the part of employers and as a hindrance to establishing bona fide, independent labor unions.[56] Under such an interpretation of law, it is hardly possible for labor and management to develop a corporate governance structure that respects employee participation.[57] In this sense, American law only allows adversarial labor relations through formal collective bargaining systems by exclusive representatives certified under the National Labor Relations Act.

Compared to the situations in Germany and the United States, the Japanese stakeholder model is unique in its non-interventionism. Restriction on dismissals is not provided by legislation, but by caselaw, and the caselaw itself was established in the interplay with the long-term employment practice. Internal management promotion or acceptance of directors-with-employee-function into the management board is simply a practice. Joint labor-management consultation is not required by law, but established and maintained by the parties' voluntary action. This is a significant difference between the Japanese stakeholder model and the German institutionalized stakeholder model.

## III. CORPORATE GOVERNANCE AND LABOR RELATIONS IN JAPAN: NEW DEVELOPMENTS AND FUTURE PROSPECTS

To reiterate, the Japanese stakeholder model of corporate governance is not established by legislation, but rather relies heavily on customary practices. Compared to institutionalized corporate governance models, the non-institutionalized model is vulnerable to environmental changes. Of course, a socio-economic system consists of several institutions and these institutions are interdependent.

56. This interpretation was established in NLRB v. Cabot Carbon Co., 360 U.S. 203 (1959) and still maintained by the NLRB and Federal Courts. *See* Electromation Inc., 309 N.L.R.B. 990 (1992); E.I. duPont de Nemours & Co., 311 N.L.R.B. 893 (1993); Polaroid Corp., 329 N.L.R.B. 47 (1999).

57. In the 1990s, there were several attempts to modify the interpretation or amend regulations such as the "Dunlop Report " (Commission on the Future of Worker-Management Relations, Report and Recommendations) and proposals called the TEAM Act (Teamwork for Employees and Managers), but they failed.

Therefore, one system is not easily transformed into another.[58] However, in an era of disequilibria, when several institutions change simultaneously, one social system can conceivably transform into another. Therefore, the question is whether or not such systemic changes are presently occurring in Japan.

### *A. Shareholders*

As regards to shareholders, at the time of the Top Management Survey in 1999, 60% of respondents are unwilling to dissolve cross-shareholding. However, since then, such a dissolution of cross-shareholding seems to have developed steadily. The rapid increase in foreign investments in the Japanese stock market will also change the shareholders' behavior in Japan. Recent modification of corporate law to facilitate "shareholders representative suits"[59] require more "shareholder-value conscious" corporate governance. After the collapse of bubble economy, together with a shift from indirect finance via banks to direct finance, the importance of Japanese banks in corporate governance has been reduced. In these situations, it is no surprise that shareholder value has surfaced as a new criterion.

### *B. Management*

In terms of management, under Japan's unique dual monitoring system by the board of directors and auditors, a traditional measure for enhancing the monitoring mechanism was to strengthen auditor power and independence. However, as previously noted, a more fundamental reform—to abolish the auditor system and adopt an American-style "board of directors" system utilizing non-executive directors—recently was proposed by the Corporate Governance Forum of Japan. This proposal was mostly accepted in the interim draft on the revision of the Commercial Code (hereinafter "interim draft")[60] by the Legislative Council of the Ministry of Justice (*Hosei Shingi Kai*), an advisory council to the Minister of Justice.

The interim draft points out the defects of the current board of directors system. As for the idea of the monitoring system, it is said to have an inherent defect in that monitors themselves engage in

58. MASAHIKO AOKI & MASAHIRO OKUNO, KEIZAI SHISUTEMU NO HIKAKU SEIDO BUNSEKI (COMPARATIVE INSTITUTIONAL ANALYSIS OF ECONOMY) 1 (1996).

59. In order to facilitate shareholders' representative suits, the 1993 revision of the Commercial Code fixed the filing fee at a nominal amount (8,200 yen), which was escalated according to the amount claimed previously.

60. The interim draft was issued on April 18, 2001, and is *available at* http://www.moj.go.jp.

corporate administration. As for practice, the number of directors is said to be too large to function effectively. Moreover, most are directors-with-employee-function and thus they are *de facto* subject to the representative directors. To cope with these problems, the interim draft states that it is necessary to separate the monitoring mechanism and corporate administration in order to strengthen the former, to delegate the power to executive officers (*Shikko-yaku*) in order to enhance the business operation and, to establish three committees (an audit committee, an appointment committee and a remuneration committee) in order to enhance the monitoring mechanism's independence from the board of directors. If firms adopt the audit committee under the board of directors, they will not be required to nominate any auditors. There must be more than three directors on these committees and the majority of these must be outside or non-executive directors. Irrespective of the adoption of these committee systems, large companies must appoint at least one non-executive director.

The new committee system is optional, not compulsory. Companies can maintain the current dual monitoring system. However, if the company wishes, it may adopt this American-style board of directors system instead of the current dual monitoring system.

Since the interim draft is not a finalized proposal, but rather a tentative draft subject to modifications, it is too early to evaluate its real impact on corporate governance structure. However, if this proposal is adopted and passed at the Diet, it will be one of the most fundamental revisions in post-war corporate law history.

### *C. Employment and Industrial Relations*

Employment is becoming more unstable and atypical or non-regular employment is increasing. Ten years ago, non-regular employees made up 20.2% of the Japanese work force, but by 2000, this had risen to 26.2%. To cope with the increased lateral mobility, the Japanese government provided a series of measures to activate the external labor market.[61] However, according to the Top Management Survey, few senior managers believe that long-term employment practices will change drastically over the next five years. Liquidation of the labor market will proceed, but modification of long-term

61. Takashi Araki, *1999 Revisions of Employment Security Law and Worker Dispatching Law: Drastic Reforms of Japanese Labor Market Regulations*, 38-9 JAPAN LAB. BULL. 5 (1999).

employment practices will be a gradual process. After the collapse of the bubble economy, it is evident that Japanese corporations can no longer maintain both long-term employment and the seniority-based wage system. According to various opinion surveys, a *de facto* consensus exists between management and labor to preserve long-term employment and, for that purpose labor has started to accept radical modification of the seniority-base wage system. There have been no drastic changes in industrial relations. However, union density is declining continuously (currently 21.5% as of 2000) and voluntarily established joint labor-management consultation faces some problems.

As for the relationship between collective bargaining and labor management consultation, European countries typically have dual systems with industry-level collective bargaining by unions and companies or plant level consultation by works councils. In Japan, however, the demarcation between joint consultation and collective bargaining is blurred because both take place at the same level, by the same parties and on the same subjects.[62] Such a vague distinction leads to an informalization of collective bargaining. Usually, joint consultation occurs prior to collective bargaining and when the parties reach an agreement through consultation, there is no need to proceed to collective bargaining, making joint consultation a replacement for collective bargaining.

In this context, it is important to note that voluntary joint consultation has been encouraged by the sanction of a union's right to bargain. If the union is treated with hostility and the employer does not take its opinions into consideration, the union can at any time terminate joint-consultation and initiate collective bargaining, wherein unions can resort to economic weapons. The union decides whether or not to maintain such cooperative consultation practices. The bitter experience of severe confrontation between labor and management in the 1950's and 1960's, when radical socialists led the labor movement, remained fixed in the memory of employers at least through the 1980s. However, in accordance with the stabilization of Japan's industrial relations and the increase in managers with no experience of harsh labor management confrontation, the incentive to engage in voluntary joint consultation seems to be declining.

When labor and management lose sight of the ultimate objective and do not fully engage in earnest joint consultation, it can become a mere formality. Some such signs were witnessed in the 1990's, after

62. Japan Ministry of Labor, *supra* note 45.

the collapse of the bubble economy. For instance, the 1999 report of the Japan Productivity Center for Socio-Economic Development,[63] a think-tank which is closely related to the management camp and also a main promoter of the joint labor-management consultation movement, warned of the declining function of labor-management consultation with respect to information exchange, decline in efforts by both labor and management to effectively utilize joint consultation and the declining influence of joint consultation on the actual lives of workers.

As for the internal promotion of management, the aforementioned interim draft will have a significant impact. The introduction of non-executive directors and the adoption of an executive officer system will result in a decrease in directors-with-employee-function. Thus, Japan's non-institutionalized stakeholder model of corporate governance faces various and significant challenges. Though changes in employment and industrial relations are rather gradual, the structure of shareholders and management mechanisms are each experiencing drastic modification. Though it is difficult to predict the exact impact of current changes, especially that of the proposed interim draft, it is likely that the non-institutionalized stakeholder model will undergo some modification.

To what extent the current stakeholder model changes will depend on whether new measures to institutionalize the current stakeholder model will be adopted or not. Though there are no concrete proposals for that purpose at present, many academic experts believe that a statute against unjust dismissals that requires just cause and stipulates appropriate remedies should be enacted. Moreover, ideas to introduce employee representatives to the auditor board have started to be discussed.[64] To cope with declining union membership, unions are advocating the establishment of Japanese-style works councils. The 1998 revision of the Labor Standards Law requires the establishment of worker-management committees when employers wish to utilize "discretionary work schemes," under which they are *de facto* exempted from overtime pay regulations.[65] Half of the members of the committee must be appointed by the labor union organized by a majority of workers at the workplace concerned or

63. The Japan Productivity Center for Socio-Economic Development (Standing Committee on Labor-Management Relations), *Current Situations and Issues of Labor-Management Joint Consultation* (April 8, 1999), *available at* http://www.jpc-sed.or.jp/index.html.

64. Junjiro Mori, *Kaishahogaku no Saikochiku ni Mukete*, 1535 SHOJI HOMU 18 (1999).

65. Ryuichi Yamakawa, *Overhaul After 50 Years: The Amendment of the Labour Standards Law,* 37-11 JAPAN LAB. BULL. 5 (1998).

with the person representing a majority of the workers where no such union exists. Though the jurisdiction of this committee is currently confined to working hour regulations and its establishment is not compulsory, it may be the first step toward a Japanese version of works councils.

In the past, Japanese employers and employees endeavored to strike a unique balance between their interests. For instance, to strike a balance between flexibility and security, Japanese companies have provided employment security and Japanese employees have accepted internal and functional flexibility.[66] In the corporate governance arena, there are many different stakeholders and harmonizing their interests is not at all easy. The shareholder value model might be regarded as an attempt to strike the balance by using a uniform index of the price of shares. Where the shareholder structure is highly diversified—as it is in the United States—enhancing shareholder value might well mean the realization of plural values. Yet, it remains to be seen whether the structure of the Japanese stock market will become as diversified as its American counterpart in the near future. Furthermore, it is questionable whether the shareholder value model can entirely replace the function of the worker participation system.[67] The key concept determining the relationship between Japanese corporate governance and industrial relations is employment security. As mentioned above, even though employment security regulations in Japan are gradually being relaxed, employment security remains critical. Under the employment security system, negotiation is indispensable in adjusting terms and conditions of employment and Japanese labor law have developed rules governing such internal flexibility.[68] Therefore, in the author's opinion, to the extent that employment security retains a core role, the current changes will bring forth the re-alignment of the stakeholder framework, rather than a complete transformation into the shareholder value model.

66. Araki, *supra* note 43, at 509.

67. *See* Richard Freeman & Joel Rogers, *What do Workers Want? Voice, Representation and Power in the American Workplace*, *in* EMPLOYEE REPRESENTATION IN THE EMERGING WORKPLACE: ALTERNATIVE/SUPPLEMENTS TO COLLECTIVE BARGAINING 3 (Samuel Estreicher ed., 1999); Douglas Kruse & Joseph Blasi, *Employee Ownership, Employee Attitudes, and Firm Performance: A Review of the Evidence*, *in* EMPLOYEE REPRESENTATION IN THE EMERGING WORKPLACE: ALTERNATIVE/SUPPLEMENTS TO COLLECTIVE BARGAINING 581, 618 (Samuel Estreicher ed., 1999); Sanford M. Jacoby, *Employee Representation and Corporate Governance: A Missing Link*, 3 U. PA. J. OF LAB. & EMP. L. 449 (2001).

68. Araki, *supra* note 43.