Corporate governance reform as institutional innovation: The case of Japan

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Corporate Governance Reform as Institutional Innovation: The Case of Japan

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To address the convergence-divergence debate in corporate governance, we conduct a multiple-case, multiple-level study to analyze the diffusion of governance innovation in Japan. We argue that Japanese systems of corporate governance neither fully converge to, nor completely diverge from, the Anglo-American model. Rather, Sony—the pioneer of corporate governance reforms—and its followers selectively adopted features from this model, decoupled them from the original context, and tailored them to fit to their own situations to generate governance innovation. However, we find that the spread of innovation across firms and institutional levels is far from linear and straightforward, and that other well-regarded firms raised strong opposition to the institutionalization of corporate governance reforms. Eventually, the Ministry of Justice revised the Commercial Code to legitimize different systems, which led to the emergence of diverse corporate governance practices.

Based on the results of our study, we construct an analytical framework to examine innovation diffusion in light of conflicting institutional pressures for change and continuity. Our analysis adds complexity to the convergence-divergence debate by identifying the creation of hybrid corporate governance systems and the nonlinear evolution of such systems as a result of interactions across multiple levels. We show the various degrees of decoupling from the Anglo-American model and identify the antecedents. We then extend the conventional focus of innovation research on diffusion across firms to examine diffusion across institutional levels. We also contribute to institutional theory by offering insights into organizational field formation and the conceptualization of the state in shaping institutional change and continuity.

Key words: corporate governance; decoupling; innovation; convergence; institutional theory; organizational field; the state

Introduction

There is debate among scholars of organization science, economics, law, and sociology as to whether corporate governance systems are converging to the Anglo-American model. One perspective is that convergence is bound to happen due to the competitive pressures of global capital and product markets (Coffee 1999, Hansmann and Kraakman 2001). Others argue that convergence is unlikely or limited, because corporate governance is embedded in a nation's institutional context (Bebchuck and Roe 1999) and the governance institutions of each system have sufficient flexibility to find a solution to governance problems within their path-dependent limits (Gilson 2004).

Institutional theory is particularly useful in addressing the convergence-divergence debate on corporate governance. It is a holistic perspective that takes into account the influence of market, cultural, and institutional forces in shaping organizational forms and practices (Biggart 1991, Orrú et al. 1997, Whitley 1996). Whereas the early literature of institutional theory stressed legitimacy as the aim of organizational action and primarily analyzed cultural embeddedness and institutional continuity (DiMaggio and Powell 1983, Orrú et al. 1997), more recent literature emphasizes that organizations aim to gain not only legitimacy, but also efficiency, and throws light on the existence of institutional change amid continuity (Greenwood and Hinings 1996, Scott 2001).

To empirically validate these arguments, we conduct a multiple-case, multiple-level study to analyze the diffusion of corporate governance innovation across firms and institutional levels in Japan. Japan is a particularly relevant context due to the sheer size of its economy, the strong contrast between its corporate governance systems and those of the United States, the increasing penetration of foreign portfolio investment, and the strong embeddedness of its institutions. This study provides insight into corporate governance innovation and change in non Anglo-American countries (such as those in continental Europe and Asia) that face a struggle between global capital market forces of change and deep-seated institutional practices of continuity (Ahmadjian and Okumura 2006, Buhner et al. 1998).

Based on the results, we contest both the convergence and divergence arguments. We find that Japanese corporate governance systems neither fully converge to, nor completely diverge from, the Anglo-American model. Rather, firms tend to selectively adopt features from this model, decouple them from the original context, and tailor them to fit their local contexts to generate corporate governance innovation that gains legitimacy and achieves efficiency. Moreover, institutional innovation spreads not only across firms, but also across institutional levels, which leads to institutional change at the regulatory level. However, the spread of innovation is a complex and dynamic process that is far from linear, and straightforward, and often leads to the emergence of diverse corporate governance systems.

This study makes several theoretical contributions. First, we add complexity to the convergence-divergence debate by revealing the existence of hybrid systems that blend the Anglo-American and Japanese systems as well as the complex, nonlinear evolution of corporate governance systems as a result of interactions at firm and institutional levels. Second, we extend the literature of decoupling (Meyer and Rowan 1977; Westphal and Zajac 1998, 2001) by showing the various degrees of decoupling from the Anglo-American model and then identifying the antecedents. We also go beyond the conventional focus of innovation research on the diffusion of innovation across firms to examine diffusion across institutional levels, and in so doing show how organizations can influence their environment, which complements the conventional focus on the impact of environment on organizations. Finally, we make a twofold contribution to institutional theory. First, we illustrate the formation of contesting subfields and complex interactions across levels in an organizational field, which we believe to be more accurate in depicting organizational and institutional life. Second, in contrast to the polar (active versus passive) conceptualization of the state and the simplistic conception of its identity, we argue that the state has a double identity as both an insider in the organizational field and an outsider in the subfields, and that it is hence active, but not necessarily coercive, in intervening in corporate governance systems.

This paper consists of four sections after the introduction. In the first section, we identify the gap in the existing literature and lay out the conceptual foundation for our empirical analysis. In the second section, we describe the research focus, design, case context, data collection, and analytical methods. In the third section, we review the pressures for and against change in corporate governance in Japan, and report the diffusion of corporate governance innovation across firms and levels. In the final section, we provide an analytical framework that emerges from the study, a summary of the theoretical contributions, and future research directions.

Literature Review and Conceptual Foundation

The Organizational Field

Institutional theories generally focus on field-level phenomena (Dacin et al. 2002). DiMaggio and Powell (1983, p. 148) define an organizational field as comprising "those organizations that, in the aggregate, constitute a recognized area of institutional life." Scott (2001, p. 84) clarifies it as being "a community of organizations that partakes of a common meaning system, and whose participants interact more frequently and fatefully with one another than with others outside the field." Often, authors conceive organizational fields on the basis of technologies or markets. However, Hoffman (1999, p. 352) introduces an issue-based view of the organizational field, suggesting that "a field is formed around the issues that become important to the interests and objectives of a specific collective of organizations." He argues that conceptualizing a field centered around issues rather than networks illuminates greater complexity in field formation and development. Studying the history of chemical industry environmentalism in the United States between 1960–1993, he highlighted that chemical producers disregarded the problem of pesticide toxicity, but were pressurized into a field-level dialogue with conservation groups, government agencies, and scientific organizations. He analyzed the field membership and structure through their social interaction by examining the pattern of organizational interactions in the legal process. He revealed how the contest between competing institutions led to regulative, normative, and cognitive changes that resulted in rapid structural, technical, and cultural changes in corporate behavior. Such changes are witnessed in the shift from attempts to control pollution at industrial facilities in the 1970s to include concerns for altering raw materials and product choices in the 1990s, and to concern for sustainable development in the coming decade. Hoffman's analysis shows how an issue is "institutionally redefined, culturally reframed, and organizationally acted on" (Hoffman 2001, p. 138).

In this study, we use Hoffman's issue-based definition of an institutional field rather than the conventional industry-based view for two reasons. First, corporate governance is an issue of general concern, especially for large, publicly listed companies, and hence is not limited to any particular industrial field. Second, the industrial fields in Japan, which serve as the context for this study, are heavily interlinked by diversified intercorporate groupings, and there is a low level of interindustry variation in institutional norms, including those of corporate governance.

Consistent with the sociological perspective of the institution as a multilevel phenomenon (Scott 2001), we perceive the field of corporate governance to be comprised of actors at multiple levels, including large listed corporations, professional and industry associations, and the state. Our empirical exploration shows that these three actors play a more direct role in influencing the debate on corporate governance in Japan than other actors such as the media and academia. We thus identify them as central to our analysis. We perceive that the organizational field of corporate governance provides a forum for dialogue between actors across levels to contest and negotiate the issue of reforms. Specifically, we wish to extend the existing focus on field formation (Meyer 1982) to encompass development and change in organizational fields to reveal the possible tensions, conflicts, and negotiation that take place between contesting actors (Hoffman 1999).

Institutional Continuity and Change

Scott (2001, p. 48) defines institutions as "social structures that have attained a high degree of resilience" that are "composed of cultured-cognitive, normative, and regulative elements." North (1991) argues that institutions are both formal and informal rules that constrain human interaction in a society. Similarly, Fligstein (1996) defines institutions as shared rules that can include laws and collective understanding. These definitions share the notion that institutions provide a framework or structure for social interaction, and thus make social order possible by reducing uncertainty. Hence, institutions tend to reinforce the continuity of established systems, behavior, and practices.

However, institutions are also subject to change due to external and internal pressures (Greenwood et al. 2002, Oliver 1992, Scott 2001). Institutional change is a process that entails change in the formal and informal rules of human interaction and in the enforcement mechanisms of such rules (North 1990), or the deinstitutionalization of existing institutional forms, which may be followed by the emergence of new forms, norms, and practices (Czarniawska and Sevón 1996, Scott 2001). Oliver (1992) distinguishes the functional, political, and social sources of institutional change. In terms of corporate governance, functional pressures occur when external or organizational conditions (for example, performance downturns or an emphasis on shareholder value orientation brought about by changes in financial market structure) call into question the appropriateness or usefulness of existing practices or beliefs. Political pressures evolve through shifts in the interests and balance of power among key players because laws and regulations often reflect the interests of the most influential forces in society (Fligstein 1996). Regulatory changes may have a significant effect on resource dependency because formal rules promote only certain kinds of exchange (North 1990). For example, by facilitating access to new sources of capital or establishing new stakeholder interests, regulatory changes can lead to changes in the role of major corporate governance stakeholders (Aguilera and Jackson 2003, Fligstein 1996). Social pressures stem from changing social expectations and the emergence of a greater diversity of beliefs and practices within a society. The widespread attention that is given to corporate governance has increased the awareness of standards of "good governance," which have been increasingly formalized in codes of practice (for example, those of the British Cadbury Commission, the California Public Employees' Retirement System (CalPERS), the Organization for Economic Co-operation and Development (OECD) and the like).

Institutional pressures need to be "interpreted, given meaning and responded to by actors within organizations" (Dacin et al. 2002, p. 48). Nevertheless, the process of institutional change is complex because competing institutional regimes often coexist (Leblebici et al. 1991, Townley 2002). Deinstitutionalization does not necessarily lead to convergence or consensus on an alternative model, and its outcomes depend on interactions between numerous actors (Soule and Olzak 2004). In a transitional period when institutional standards are uncertain, individual actors and organizations may try to influence practice (Goodrick and Salancik 1996). Thus, to understand the complex process of institutional change, we need to analyze not only external pressures, but also the responses of locally embedded actors.

Decoupling and Local Tailoring

Weberian institutionalist scholars tend to adopt a relatively active view of human action, and presuppose that actors acting under institutional constraints make choices to fit their purposes (Orrú et al. 1997). Such scholars take a balanced approach, acknowledging forces of continuity and pressure for change and attempting to document and analyze the coexistence of institutional continuity and change (Ahmadjian and Okumura 2006, Tsui-Auch 2005).

The major process that brings about the contentious coexistence of institutional continuity and change is that of decoupling (Meyer and Rowan 1977), which is often complemented by the process of local tailoring (Westney 1993). On encountering external pressure for change, organizations may import foreign models but decouple them from their original institutional context and modify them to fit their own institutional contexts. Westney (1993) uses the example of multinational corporations to show that firms that face different isomorphic pulls (from home country and host country) tailor imported models to fit the local context. In terms of corporate governance, several studies show that firms in Germany proclaimed to support a shareholder value orientation but did not in fact do so (Fiss and Zajac 2004), or announced the implementation of an executive stock options program but executed it differently to suit the local institutional context (Buck and Shahrim 2005).

We agree that institutional change is a complex process, and that change and continuity coexist. However, we find that the literature is largely limited to illustrations of the decoupling process (Westphal and Zajac 1998, 2001) or the formation of a hybrid system once foreign systems have been learned (Chang 2005). Ahmadjian and Okumura (2006) remind readers of the inadequacy of simply saying the emerging Japanese system will be a hybrid of Anglo-American practices and the postwar Japanese system since such a hybrid can take various forms. It would appear that the different forms of hybrids with their various degrees of decoupling merit further exploration. It is also unclear as to the kinds of firms that will learn from foreign models, such as firms with high rates of foreign ownership or with a high degree of globalization of investment, and the circumstances under which this learning will take place. Thus, the antecedents of decoupling remain to be identified. This study takes an initial step to fill this gap in the literature.

Imitation as Innovation

Learning from foreign models evokes the debate on imitation versus innovation: the former traditionally being viewed as adaptive behaviour and the latter as creative behaviour (Fiol and Lyles 1985). An increasing number of scholars, however, conceptualize the imitation of practices and ideas developed elsewhere, and their modification to fit local contexts, as being inherently creative and innovative (Czarniawska and Sevón 1996, Hobday 1995, Westney 1993). Czarniawska and Sevón (1996) reject the conventional negative image of imitation as mechanistic copying, and borrow the metaphor of "translation" from Latour (1986) to reveal the creative nature of imitation. Translation is literally an act or process by which a text in one language is rendered in another, and is a way of expressing something in another medium or form. It involves transformation, modification, change, renovation and identity construction, the blending of the foreign and the local, the new and the old. Czarniawska and Sevón (1996) argue that, as with translation, the recontextualization of ideas that have been extracted from their original context during the process of organizational imitation requires creativity. Similarly, Westney (1993) highlights that the process of local tailoring by multinational corporations constitutes organizational innovation.

The conventional literature of innovation views it singularly in terms of the introduction of new products, technologies, or business models, and thus ignores the incremental process that leads to innovation. We, however, adopt the view that creative imitation, which involves the modification and recontextualization of context-dependent norms and practices to fit the local context, is itself innovative. In addition, we go beyond the literature of organizational imitation and innovation, which focuses on the organizational level of analysis and the impact of environment on organizations (DiMaggio and Powell 1983, Hobday 1995, Leblebici et al. 1991), to study innovation across levels and the impact of organizations on the environment.

Research Focus and Methods

In this study we first identify the forms that hybrid systems of corporate governance can take, and explain why some features of corporate governance are changed but others retained. Second, we explore the degree of decoupling that occurs in different firm contexts and identify the antecedents of decoupling. We then analyze innovation across the firm and regulatory levels. Finally, we examine the formation of the organizational field and subfields of corporate governance, with specific attention to the roles of the pioneering firms, advocates, and opponents at the firm, intermediate association, and state levels.

Research Design and Case Context

For this study we use qualitative research design, which is congruent with the emergent nature of our knowledge of institutional change in corporate governance (Maguire et al. 2004, Miles and Huberman 1994). We chose a multiple-case, multiple-level study design because it enhances complex and dynamic analysis and permits the induction of a richer and better-grounded framework than a single-case, single-level study (Eisenhardt 1989, Yin 2003).

In a qualitative research design, case selection is purposive. We selected two cases based on criteria derived from our literature review and documentary research. Ahmadjian and Okumura (2006) observe that young, innovative companies with a high proportion of foreign ownership undertake corporate governance reform earlier than more established and traditional companies that are often affiliated with one of the *keiretsu* groups. In essence, the corporate age, organizational culture, and structures (financial, ownership, affiliation) each plays a role in shaping corporate governance systems. Moreover, our vigorous documentary research reveals that large, listed firms across industries have increasingly undertaken corporate governance reforms. We therefore chose Sony and Toshiba—two large, listed firms with differences in corporate age, organizational culture, and financial, ownership, and affiliation structures—for our study. Sony and Toshiba present interesting contrasts in terms of their positions in the business community and the exposure to foreign markets. Sony operates outside of the mainstream due to its high proportion of foreign ownership, relatively young corporate age, independent status with no affiliation with any *keiretsu* group, and innovative culture. Toshiba, in contrast, is an old, traditional company with a strong affiliation with one of the large *keiretsu* groups. We expect that these factors strongly affect the degree of institutional embeddedness and the exposure to external institutional pressures. In addition, Sony is a pioneer of corporate governance reform in Japan (Suenaga and Fujikawa 2004), whereas Toshiba is a follower in governance reform in the same industry where they compete fiercely. The research into Sony was facilitated by its role as a pioneer of governance reform, which has received much attention both in Japan and abroad. This means that documentary sources are abundant, which enabled the triangulation of data.

We have supplemented these two well-known cases with two other companies that have been followers of corporate governance reforms. These cases are used for illustrative purposes and to allow us to explore the diffusion among less visible firms that makes major institutional change possible. These two firms were among the companies introduced by the lead author's industry contacts, and they will remain anonymous as per the preference of the respondents. These respondents were more willing to reveal information and opinions on corporate governance reforms than their counterparts in other companies. One firm has extensive international operations in specialized glass production and belongs to one of the large *keiretsu* groups. The other firm, in the food industry, operates primarily in the domestic market and does not belong to any *keiretsu* group. The data of these two firms further illuminate the motives of and concerns about corporate governance reforms that are uncovered in the cases of Sony and Toshiba.

Data Collection

Data collection was based on an interview guide (see Appendix) that included sections covering firm characteristics, corporate governance reforms, the motivations and factors behind such reforms, field interaction, the organizational outcomes of such reforms, and the possible future direction of corporate governance practices. The interview guide permitted the collection of both factual information (for example, dates, events, incidents, policy, and actors involved) and open-ended narrative data.

The documentary research, field preparation, rapport building with potential respondents, interviews, and analysis lasted from 2002 to 2005. The lead author, who is a native speaker, had the necessary ethnic identity, language background, and extensive corporate connections to build a good rapport with the potential interviewees. The case study was conducted in two parts. In the first part, interviews were conducted to help identify the scope of the study and to obtain referrals to appropriate respondents. The second part consisted of corporate visits, the collection of archival material, and informal and formal interviews. We identified as informants senior executives in corporate planning, law, and investor relations who were knowledgeable about the corporate governance systems and practices of their firms. These executives were selected based on formal, snowball, and opportunistic sampling methods. In accordance with informant preference, the interviews were taped or hand recorded and then transcribed. The initial interviews lasted from one to two hours, and the follow-up interviews were conducted through e-mail.

We adopt the approach of Schweizer (2005) to address the typical concerns over the qualitative research design. To enhance construct validity, we relied on the triangulation of the data with other sources whenever possible (Yin 2003). Secondary data covers corporate governance (structure and reform measures), firm characteristics (ownership structure, *keiretsu* affiliation, corporate history, industrial environment, and exposure to foreign markets), and field interaction on corporate governance reforms. They were obtained from the academic literature; the annual reports of firms; reports from government, banks, research institutes, and industry and professional associations; biographies; business daily newspapers such as *Nihon Keizai Shimbun*; and business journals such as *Nikkei Business*. External validity was improved by a comparative analysis of data across firms. Internal validity was boosted by actively seeking clarification of the answers given in the interviews and maximizing the internal consistency of the interviews. The issue of reliability was addressed by enforcing a detailed case study and interview protocol, and by setting transcription standards. We addressed informant bias through the use of multiple respondents and both retrospective and real-time data. The use of retrospective accounts facilitated the collection of more observations (hence giving a better grounding), and the collection of real-time data reduced retrospective bias (Eisenhardt 1989). We assured the anonymity of both informants and the firms to promote candor, and report only the names of Sony and Toshiba, with the consent of the informants.

Data Analysis

The grounded theory-building approach (Glaser 1998) guided us from an interpretive analysis of content to the construction of an analytical framework through five steps. In Step 1, we performed content coding of the interview transcripts and data from the secondary sources to create an organized interpretation of the data. In Step 2, we conducted a within-case analysis using a matrix technique of comparative analysis across the interviews within each case (Miles and Huberman 1994, Schweizer 2005). The resultant detailed case description with possible causal inferences led to additional data collection (also through e-mail) and reanalysis. In Step 3, we analyzed the factors and motivations behind the imitation of Sony's reform among other enterprises, and identified the different circumstances that led to the different degrees of decoupling. We then traced the spread of innovation across firms and regulatory levels, with particular attention to the actions of firms, intermediate associations, and state agencies. Finally, in Step 5 we formulated a conceptual framework to show the relationships between constructs and patterns. The explanations were refined through replication logic and the frequent revisiting of the data. The iteration between theory and data aided the fine-tuning of the constructs, and enhanced the internal validity of the findings and the development of the most defensible arguments (Eisenhardt 1989).

Corporate Governance Change and Innovation: The Case of Japan

The Japanese business system is characterized by tight networks of vertical and horizontal groupings that are known for their cross-shareholdings and other financial ties (Gerlach 1992). Instead of owning stock primarily for investment purposes, investors are often the banks or trading partners of a firm that hold shares to express business goodwill, information exchange, and mutual monitoring (Kester 1991). Consequently, the boards of directors of many Japanese firms have traditionally paid little attention to the interests of nonaffiliated investors.

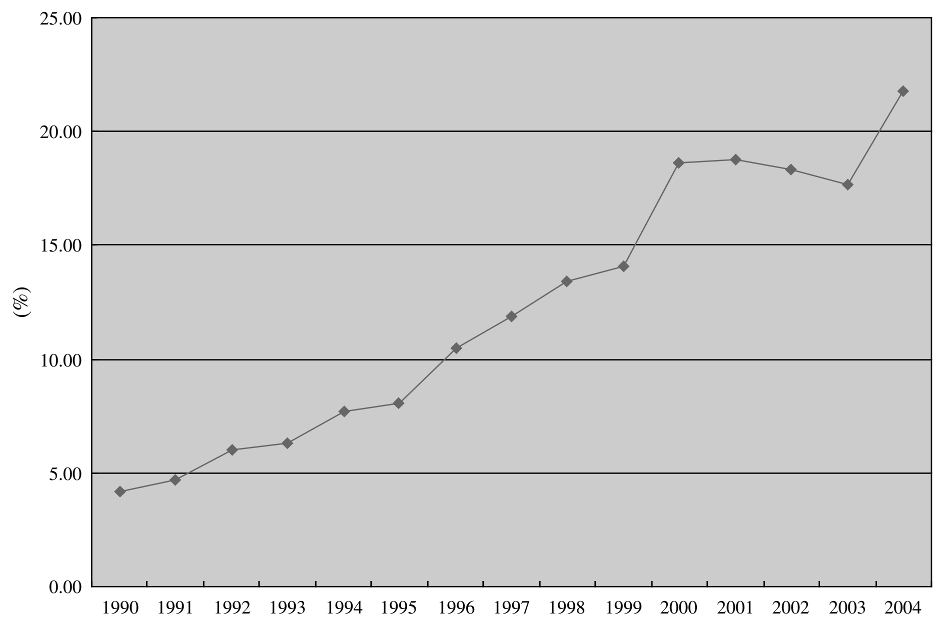
Most Japanese boards are composed primarily of insiders who have been promoted from within the company (Charkham 1994). A directorship is considered a reward for an employee who has survived a long internal competition (Gerlach 1992). To serve this purpose, most boards are large, with some consisting of as many as 60 members. Board members are often viewed as de facto managers who are subordinate to the president or CEO. The few outside directors, if any, are mostly drawn from the main banks, trading partner firms, or supervising government ministries (Westney 2001), and hence lack independence from the management. Due to the limited separation between the director and executive positions, Japanese boards do not play a primary role in the monitoring of top management (Charkham 1994, Heftel 1983).

Institutional Pressures for Change and Continuity

The globalization of stock investment by institutional investors and relatively cheaper Japanese equity prices following the bursting of the bubble economy in the 1990s led to a significant increase in foreign portfolio investment by market value in Japan from about 4% in 1990 to 22% in 2004 (see Figure 1) and a concomitant decline in shareholding by domestic affiliated investors from over 45% in 1990 to 24% in 2003 (NLI Research Institute 2004). These foreign investors are predominantly institutional investors from the United States and the United Kingdom that made up 41.8% and 30.9% of foreign shareholdings, respectively, in 2003 (Bank of Japan 2004). Seeking a high investment return, foreign investors tend to trade shares more frequently than domestic institutional investors, which affects the share price of Japanese firms and, subsequently, their strategic decisions and performance, despite the fact that these investors usually only hold a small block of shares (David et al. 2006, Nitta 2000).

At the same time, traditional reliance on bank financing is diminishing, with the increasing use of nonbank debt among both group-affiliated and independent firms (Hodder and Paker 2002). Changes in foreign exchange

Figure 1 Foreign Ownership in Japanese Firms (by Market Value)



Source. *Kabunushi Bunpu Chosa* (Survey on stock distribution). The Association of Stock Exchanges, 2005.

controls have allowed Japanese firms to issue unsecured foreign bonds, and this access to foreign capital has been accompanied by growth in the local bond markets. Both trends have reduced dependence upon traditional stakeholders of corporate governance.

Under these circumstances, functional, political, and social pressures for change in corporate governance have emerged. Functional pressure has increased as a result of well-publicized financial and corporate governance failures during the prolonged Japanese economic slowdown, rising competition in the financial and product markets, and expectations of the adoption Anglo-American practices on the part of foreign shareholders (Yoshikawa et al. 2006).

Social normative pressure has amplified with the rapid diffusion of corporate governance codes (such as those proposed by CalPERS and the OECD) that legitimize the notion of shareholder value (Jackson 2003). Access to a wider range of financing options due to financial liberalization has also weakened the dependence of many firms on traditional stakeholders while raising their dependence on institutional investors who have pressured Japanese firms to adopt Anglo-American standards of corporate governance (Useem 1998). For example, CalPERS (2004), which is well known for corporate governance activism, proposed the appointment of independent outside directors and the reduction of board size to promote efficiency and responsiveness. Similar to the processes that are observed by Fiss and Zajac (2004) among German firms, Japanese firms have increasingly sought legitimacy by endorsing shareholder value in their annual reports (Jackson 2003).

Finally, political, coercive pressure has emerged from external political forces and changes in resource dependency and stakeholder relevance. In response to pressures from the U.S. government for greater shareholder protection, the Japanese government revised the Commercial Code in 1993 to facilitate shareholder litigation (Dore 2000, Keidanren 1996). Changes in corporate financing practices have further altered traditional stakeholder dependency.

However, amid the numerous forces of change are entrenched forces of institutional continuity. One is the culturally embedded view that a firm, which is a community of people or employees, belongs to its employees, not to its shareholders (Dore 2000, Itami 2000). This view contrasts with the notion of shareholder supremacy in the U.S. model of corporate governance. Despite a prolonged economic downturn, large Japanese firms such as Toyota and Canon have continued to value employment security as a source of competitive advantage for Japanese firms (Nikkei Global Management Forum 1999). Another force of continuity is the entrenched norm of trust in insiders. Because a firm is a community of employees or insiders, any move to bring in outside directors for the purpose of monitoring the top executives, who are insiders in the community, generates strong resistance. In addition, the aspiration of top managers for a seat on the board creates further pressure against change (Jackson 2003). Obviously, the insider-oriented and employee-focused system has remained entrenched.

Sony and Its Corporate Governance Innovation

The field of corporate governance in Japan has evolved in the context of increasing institutional pressure for change on the forces of continuity. Sony's corporate governance innovation is the distinguishing event in the development of the field, and its innovation has spread across firms, thus giving further impetus for regulatory reforms.

The Sony Corporation was founded in 1946 by Masaru Ibuka and Akio Morita, and gained domestic recognition for its product innovation and pioneering spirit in the 1950s. As a relatively new firm, it was positioned on the periphery of the domestic corporate sector, which was dominated by the prewar *zaibatsu* firms. The founders saw a greater opportunity to grow in foreign markets, especially in the United States (Fruin 1992), than in the domestic market, and thus opened its first overseas office in New York in 1957. Lacking close ties to the prewar *zaibatsu*, Sony encountered difficulties in obtaining financing from domestic banks, particularly in the early years (Morita et al. 1986, Sato 1995). Hence, it became the first Japanese company to issue American Depository Receipts in 1961 and to list its shares on the stock exchanges of New York, London, and Amsterdam in 1970. It appointed two outside directors to its board after listing its shares on the New York Stock Exchange, and invited a non-Japanese to be an outside director in 1991, which was an innovative move for a Japanese firm at that time.

With the downturn in its finances due to the poor performance of its movie division (Columbia Pictures, which Sony acquired in 1989) after 1994, and the prolonged Japanese economic recession, Sony was under pressure to improve its performance. At the same time, its foreign ownership increased from 15.3% in 1990 to 33.3% in 1996 (see Table 1). Although the then Vice Chairman Tsunao Hashimoto officially denied any direct pressure from external sources, it was clear that the international capital markets had at least an indirect effect on Sony's move to reform its board.

> There was no direct pressure [from foreign investors to reform its governance]. However, since investors are crossing national borders, we thought it was easier for them to buy our securities if they could understand our management system.... Transparency is very important in a market economy.... A board system that can be accepted internationally is required. Otherwise, investors get worried. (*Nihon Keizai Shimbun* 1998)

Table 1 Foreign Ownership (%) in Sony and All Listed Japanese Firms (by Unit Shares Held)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Sony	15.3	18.8	21.6	24.4	30.6	27.0	33.3	39.0	45.0	45.1	44.5
All	4.2	5.4	5.5	6.7	7.4	9.4	9.8	9.8	10.0	12.4	13.2

Source. Sony Corporation. The Association of Stock Exchanges, 2005.

In 1997, Sony began to adopt the *shikko yakuin sei*, or corporate executive officer system (EOS). In the EOS, the roles of executive officers and directors are separate, and the board size is reduced (Nikkei Business 1998). Tsunao Hashimoto revealed the factors behind, and the objective of, this adoption as follows. "By doing it, we, as a group, can improve our capability to monitor business decision and implementation" (Hashimoto 1997, p. 9).

Although Sony's new boardroom practices were reported in the media as being a step toward the U.S. model (Komiyama and Masaoka 2002), there were still important differences between the board structure of the EOS and that of U.S. firms. Although Sony reduced the number of directors from 38 to 10, insiders continued to dominate the board, with only three outside board members. There remained an overlap in the roles of executives and directors, because all of the insider directors were also corporate executives. After initiating the EOS, Sony established compensation and nominating committees—modeled on similar committees among listed U.S. firms—in 1998, and an outsider-dominated advisory board in 2002. However, although the compensation committee was led by two outsiders, the nominating committee was dominated by insiders, whereas in listed U.S. firms these committees are usually dominated by outside directors. The advisory board gave outsiders only advisory roles rather than decision-making roles. These practices clearly indicate a decoupling from the U.S. model and its tailoring to fit the local domestic context. A report from *Nikkei Business* commented: "Sony's board consists of mostly insiders and hence it does not really reflect the U.S. model.... Its practice is Japanese- or Sony-style (1998, p. 45)." Nobuyuki Idei, Sony's former chairman and CEO, contested the global or, more accurately, Anglo-American, standards (Idei 2004):

> I think there is no such thing as "global standards" in corporate governance. If there are any standards, they reflect a different history of capitalist development.

This decoupling from the Anglo-American model was driven by a strong trust in insiders, which is seen to generate not only legitimacy, but also efficiency. Sony's senior executives regarded the reliance on insiders rather than outsiders as less time-consuming and less costly, because the insiders had more management experience with, and information about, the company than the outsiders. Teruo Masaki, Sony's senior executive vice president and vice chairman of the board stated:

> We expect outsiders to provide sound general judgment on strategic issues.... But there is sometimes a perception gap between those who have managerial experience and other professionals without any managerial experience.... The company needs to provide more detailed information and data to those outsiders without any managerial experience, and that could be costly.

Diffusion of Innovation Across Firms: A Different Degree of Decoupling

In the mid-1990s, supporters of corporative governance reforms were primarily firms that operated outside the mainstream, such as Sony and Hoya. By 2005, even large mainstream companies with *keiretsu* affiliations and firms with limited exposure to global capital or product markets and good financial performance had adopted the EOS. In 2005, 645 out of a sample of over 1,300 firms had adopted the system (see Table 2), which was seen as the biggest hit since Sony invented the "Walkman" (*Nihon Keizai Shimbun* 1999).

Similar to Sony, Toshiba experienced a significant decline in profits in 1998, and was beset by "a sense of crisis over its diversified structure of electronics businesses" (*Nikkei Business* 1998). A manager recalled that Sony presented a convenient model for Toshiba to emulate:

> The EOS was started by Sony.... That was one of the triggers.... Sony started this [EOS], and then quite a number of other companies in this industry followed. Companies in our industry adopted it because we were competing not only within Japan but also in overseas markets, hence we needed to improve our competitiveness.

In addition, Toshiba faced social pressure from foreign investors to reform its corporate governance despite their

Table 2 Diffusion of the Executive Officer System

Year	Sample size	Number of firms*	Ratio (%)
1997	NA	1 (Sony)	NA
1998	1,137	40	3.5
2000	1,310	279	21.3
2002	1,363	466	34.2
2005	1,317	649	49.3

Source. Tokyo Stock Exchange, 1998, 2000, 2003, 2005.
*The number of firms that have adopted or decided to adopt the EOS.

lack of belief in its impact on performance, as a senior manager remarked:

> As we have large overseas sales and overseas business activities and we also have many foreign investors, it is not sufficient if we only stick to the Japanese model. Therefore, although we don't think that we will succeed by importing the pure U.S. model, we would like to move toward a model that is valued highly by foreign investors.

Indeed, firms were compelled to restructure their governance and management structure to meet the most dominant corporate governance standards. A senior manager of a major glass company that had adopted the EOS explained the situation as follows.

> In order to become a global blue-chip company, we need to... manage the firm with global teams... we need to reform our management structure.... One part of the structure is corporate governance... we need to separate board members from executives.

Like Sony, these companies adopted the EOS and reduced their board size, but neither made a clear separation of the monitoring and executive functions, nor established an outsider-dominated board structure like listed companies in the United States. Trailing Sony's move by two years, Toshiba established nominating and compensation committees in 2000, but few other companies followed suit, which indicates a high degree of decoupling from the Anglo-American model. The resulting hybrid system, which blended the form of the U.S. system and the substance of the Japanese system, is depicted as follows by a senior manager of Toshiba.

> What we have probably looks like the U.S. model. In actual practice, however, we don't have a board that consists only of independent outside directors. We have overlaps between directors and executives.... If we really separate monitoring and executive functions, we cannot manage the firm.... Since we require linkages between directors and executives, there are joint appointments. We are not aiming to increase outsiders and to decrease joint appointments with executives in the near future.

Such decoupling from and local tailoring of the U.S. model was motivated by the high trust in insiders, belief in the benefits of executive board links, and doubts about the effectiveness of an outsider-controlled board. An informant from a food company expressed:

> it is not desirable to increase the ratio of outsiders on the board.... I feel that only an insider-dominated board can make the right business judgments.

The Emergence of Contesting Forces

Firms such as Orix and HOYA, which had already followed Sony in adopting the EOS, became confident in further pursuing the corporate governance reforms. In 2002 they established the Japan Association of Directors, led by the chairman of Orix, to promote the appointment of outside directors in Japanese firms (*Nihon Keizai Shimbun* 2002). However, many well-regarded (and profitable) firms with extensive foreign market exposure, such as Canon, Toyota, and Honda, raised strong opposition to the move, arguing that the insufficient number of qualified outsiders in Japan made the proposed reform impracticable (*Nihon Keizai Shimbun* 2003). They also questioned whether outsiders could make meaningful contributions due to their insufficient industrial and internal corporate knowledge (*Nihon Keizai Shimbun* 2003). The corporate governance reforms on the U.S. model were seen as inappropriate for the Japanese context. Hiroshi Okuda, the Chairman of Toyota, stated:

> Recently, a number of Japanese firms have adopted the U.S. style restructuring measures, the EOS, and outside directors, claiming that they will improve their competitiveness. These management measures were born in a context that is different from the Japanese context in terms of culture and system, and therefore such measures do not necessarily work well. (Nikkei Global Management Forum 1999)

Not only individual firms, but also professional and industrial associations, resisted the legislation of reforms. *Keizai Doyukai* (Japan Association of Corporate Executives) strongly opposed a law mandating the appointment of outside directors, as reflected in its report of 2001.

> The role of the Commercial Code is to present a menu with various models from foreign countries and our country that can be accepted internally, and each firm should be free to select and implement measures from that menu. Legal requirements should be minimized and each firm should, on its own responsibility, choose a system that is suitable for the environment in which it is placed. (Keizai Doyukai 2001)

As a compromise, *Keidanren* (Japan Federation of Economic Organizations 2000), which is an association of large corporations, called for the improvement of the traditional governance system rather than the introduction of outside directors.

Diffusion of Innovation Across Levels

The spread of the EOS across a broad range of firms gave further impetus for institutional innovation at the regulatory level. Corporate law scholars and officials from the Ministry of International Trade and Industry (MITI: now the Ministry of Economy, Trade and Industry or METI), a central actor in global trade, considered corporate governance reforms to be a means of increasing the competitiveness of Japanese firms in the global financial markets. A METI report (2000, p. 2) states the following.

> It is becoming important for corporate management to get a positive evaluation in financial markets (and stock markets), for example, by managing the firm in a manner responsive to rising foreign ownership and by acquiring a rating from rating agencies.

The Ministry of Justice (2000) recognized the problems that are associated with insider domination of Japanese boards and the globalization of accounting and legal standards, and also perceived a positive relationship between the improvement of corporate governance and national competitiveness. In the words of one of its officials:

> Just like it happened with the internationalization of the accounting standards, the internationalization of corporate law has also started to happen. To improve the country's competitiveness, we should not be left behind. (*Nihon Keizai Shimbun* 2004)

However, the Ministry faced severe tension in pursuing corporate governance reforms. Both advocates and opponents for the appointment of outside directors enjoyed the support of firms, professional and industrial associations, and state agencies, and although the institutional logic of the Anglo-American model was gaining momentum, that of the Japanese system continued to exert an influence. Obviously, there was a lack of evidence for the superiority of the outside director system, especially with the series of corporate scandals in the United States that led to the Sarbanes-Oxley act in 2002, which aimed to strengthen management accountability for financial reporting and information disclosure to the market and investors.

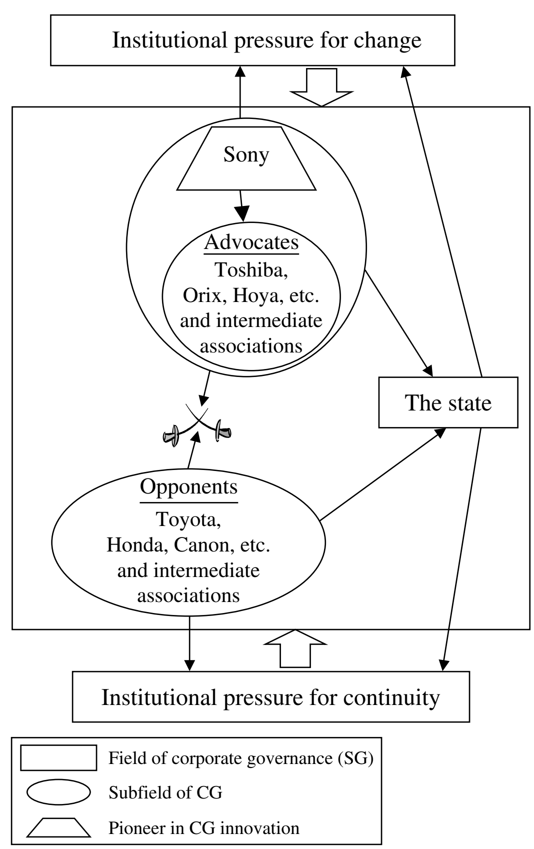
Faced with these contesting forces and competing institutional logics, the Ministry revised the Commercial Code to provide large Japanese firms with two options of internal corporate governance structure, rather than imposing a hybrid model. One of these options is to maintain the traditional system whereby a firm has a board of directors and a board of statutory auditors, the latter being responsible for monitoring that the board of directors complies with law and exercises sound business judgment. Large firms are required to have at least three statutory auditors, one of which must be an outsider. The other option is to adopt a committee system that is based on a board of directors and three committees (nominating, audit, and compensation) that resemble those established by Sony and Toshiba. In this system, which also resembles that adopted by listed U.S. firms, the board of directors is responsible for monitoring the management, and the execution function is delegated to the executive officers. The committees are supposed to include outside directors, thus providing a further separation between monitoring and execution functions. This regulatory reform reinforces the EOS that was initiated by Sony by providing a clear legal status for executive officers (Komiyama and Masaoka 2002) and enlarges the scope of Sony's committee system. This shows that innovation at the firm level has led to innovation at the institutional level.

Nevertheless, this institutional innovation signifies a more significant change from the traditional Japanese system than Sony's EOS, and firms that adopt the new system will find it more difficult to reform their corporate governance while retaining traditional insider dominance, as Sony did. Thus, when the legal revision became effective in 2003, a clear majority of firms opted to preserve the traditional system. In the first year, only 36 firms (including Sony) out of over 1,500 firms listed in the first section of the Tokyo Stock Exchange, which includes most of the large firms, adopted the committee system. This increased to about 70 firms in 2004, but so far there has been only limited diffusion of this institutional innovation.

Discussion and Conclusion

Our multiple-case, multiple-level study has led us to develop an analytical framework to examine innovation across firms and levels. As graphically presented in Figure 2, the field of corporate governance has evolved amid pressures for institutional change and for continuity. The field comprises major players, including large firms, intermediate associations, and the state. Sony played the pioneering role in effecting institutional change by implementing the EOS, and the diffusion of this system across firms such as Toshiba, Orix, and Hoya led to the formation of a subfield in which a professional

Figure 2 An Analytical Framework of Innovation Diffusion Across Firms and Institutional Levels



association for corporate governance reform was established. This subfield reinforced the institutional pressure for change. However, such a strong advocacy for corporate governance reforms aroused intense opposition from other well-regarded firms (including Toyota, Honda, and Canon) as well as professional and industry associations, and thus a contending subfield emerged to exert influence on the state and the discourse of the field. The fact that these large corporations have continued to value the insider-dominated board structure as a source of competitive advantage for Japanese firms reinforced the institutional pressure for continuity. In response, the Ministry of Justice proposed two corporate governance systems to accommodate the different demands of the two subfields, which further reinforced institutional pressures for and against change. Thus, differing corporate governance systems have emerged, with a minority of firms developing a hybrid system that resembles the Anglo-American model and a majority of firms retaining the traditional Japanese corporate governance system. The applicability of this analytical framework to other institutional contexts awaits further validation.

Theoretical Contributions

This study makes several important contributions to theory and research on corporate governance, innovation diffusion, and institutional change. Our analysis adds complexity to the convergence-divergence debate on corporate governance. In contrast to the argument (Coffee 1999, Hansmann and Kraakman 2001) that convergence is inevitable due to the competitive pressures of global capital and product markets, our data show that the majority of Japanese firms have opted to preserve the traditional corporate governance system, which is permitted and legitimized by the state regulatory agency. However, contrary to the hypothesis of the divergence argument (Bebchuck and Roe 1999) that corporate governance is embedded in a nation's institutional context, and hence convergence is unlikely or limited, we find that an increasing number of firms have locally tailored the imported model to fit their own contexts. Our study suggests that the evolution of corporate governance is more complex than portrayed by the convergence-divergence debate. We show that corporate governance change is a fluid and nonlinear evolution in response to both internal and external pressures and involves the interactions across firm and institutional levels. In response to external pressures (from the international legal and financial communities) and internal pressures (from local firms and intermediate associations), the Japanese regulatory agencies eventually allowed local firms to choose between different corporate governance models. Firms can then adopt a corporate governance model that is the most appropriate to address stakeholder demands and perceived threats to their resources and legitimacy. Our analysis of the Japanese context suggests that although regulators may be able to enact formal corporate governance change in response to pressures, corporate governance at firm level may remain embedded in the local institutional context. Such a view directs the convergence/divergence debate not only to the formal institutional arrangements, but also to firm-level governance choice and response within the formal framework.

We also go beyond previous studies that focus on the formation of a hybrid when two institutional logics meet (Chang 2005, Tsui-Auch 2005) to identify the different kinds of hybrid systems with different degrees of decoupling. As is shown by our data, although Sony adopted the EOS in 1997 and established nominating and compensation committees in 1998, most of its followers (with the exception of Toshiba) adopted only the EOS, thus exhibiting a higher degree of decoupling from the Anglo-American model and the development of a hybrid that more closely resembles the Japanese model. Furthermore, Sony's shift from the EOS to the committee system in 2003 indicates a reduction in the degree of decoupling, which provides empirical support for the argument that decoupling is an incremental process (North 1991, Sherer and Lee 2002).

In addition, we are able to identify the antecedents of learning from Anglo-American models. We argue that the exposure to foreign capital or product markets, as the advocates of the convergence argument have highlighted, may not always lead to a convergence to "global" standards. Our data show that many firms with a high level of exposure to foreign capital or product markets, such as Toyota, Honda, and Canon, rejected the U.S. model, and that although it was a factor behind Sony's adoption of the EOS, it was not the only factor—other factors such as financial performance, positioning in the business community, and organizational culture each played an important role. As for the followers of Sony, such as Toshiba, factors such as positioning in the business community were of less importance, whereas social, normative pressures played a role equally as important as financial performance and exposure to foreign markets. Interestingly, despite the contrasting factors between the pioneer and its followers, they both implemented the similar reform measures. However, we argue that the antecedents and the level of decoupling differ among pioneers and followers of corporate governance reforms.

We extend the conventional focus of innovation research on the diffusion of innovation across firms (Leblebici et al. 1991) to analyze the diffusion of innovation from the firm to the regulatory level. By so doing, we are able to show the impact of organizations on the environment, which complements the conventional focus on the impact of environment on organizations (Campbell and Lindberg 1990, Fligstein 1996). The spread of innovation across institutional levels, however, is far from linear and may bring about unintended consequences. Our data show that the Japanese state promoted reform in a way that exceeded that which was advocated by Sony and its followers, but, contrary to expectations, also legitimized the traditional corporate governance system, thus giving firms leeway to reject the institutional innovation. Obviously, the spread of institutional innovation (such as the committee system) to firms has been particularly slow, partly because it represents a clear break from traditional practices and partly because the regulatory agency permits the preservation of the traditional system. We therefore agree with Sherer and Lee (2002) that in the absence of highly visible pressures (institutional or resource-based), the existence of the option to innovate does not necessarily mean that firms will do so.

Our analysis contributes to institutional theory in two ways. First, it shows that field development, as with the diffusion of innovation and institutional change, is complex and dynamic, rather than straightforward and linear (Hoffman 1999). Pioneers and followers each have a role to play, which appears to support arguments for the roles of both peripheral participants (Durand and McGuire 2005, North 1991) and central players (Greenwood and Suddaby 2006). In addition, subfields have emerged to contest one another in the field of corporate governance in Japan, with Sony, the pioneer, and its followers (Toshiba, Hoya, and Orix) advocating corporate governance reforms, and Toyota, Honda, Canon, and other well-regarded firms resisting such reforms. Both camps built and enlarged their own subfields with the support of intermediate associations and the state that helped them to gain legitimacy. The development of organizational subfields thus generated diverse definitions of, and solutions to, issues. Our study shows that institutional change is a complex process, and that it does not proceed sequentially from one model to another due to the emergence of contesting subfields that develop and influence policy and practices (Goodrick and Salancik 1996). It is hardly surprising that such different corporate governance systems coexist in Japan given the legitimization of both by the regulatory agency (Leblebici et al. 1991).

Second, we provide new insight into the role of the state in influencing firm behavior that challenges the simplistic conceptualization of the state and its identity. Scholars who perceive the state to have a strong role in shaping institutions focus on the active, coercive nature of state intervention (DiMaggio and Powell 1983, Skocpol 1979, Tsui-Auch and Lee 2003), whereas scholars who perceive the state to have a weak or marginal role play down its importance (Hamilton et al. 2000). Our study shows that although the state has the power to impose coercive pressures over its constituents and to set formal constraints (North 1990), it is also subject to the influence of organizations and their subfields. Essentially, the state has a double identity—it is both an insider in the organizational field and an outsider in the subfields—and hence enjoys relative autonomy, but not absolute independence, from the other players. The state can play an active role, but its intervention is far from coercive. As Gordon and Roe (2004) illustrate, corporate governance reform, which often requires legal change, usually also requires political consensus and the agreement of political and corporate elites. The simplistic conceptualization of the role of the state thus needs to be revised to aid the analysis of institutional actions, especially in institutional contexts that are characterized by negotiable state-capital relations.

Limitations of the Research and Future Research Directions

As this study is based on a small sample of firms, the generalizability of the analytical framework remains to be tested. However, the focus on a small sample was necessary to explore the complex and dynamic process of innovation across firms. Also, the merit of using a small sample of cases to generate theories is increasingly recognized in organization science (Eisenhardt 1989, Schweizer 2005).

Although this study (like all other studies) is limited in scope, these limitations can serve as stepping stones to guide future research. Our study covers the period from the 1990s to 2005 during which the revised Commercial Code (including the introduction of the committee system) was implemented. Thus we can only observe the diffusion of this institutional innovation up to 2005, and do not have a full picture of its effects on firms and the institutional environment. A promising avenue for future research would be to study in greater detail the diffusion of institutional innovation to firms and the impact of such diffusion on organizations and the environment. Such research would add complexity to the analytical framework that has been generated in this study.

Our analysis is limited to the firm and institutional levels. We focus on the firm as a whole, in this case the innovator Sony, but do not explore the role of its individual leaders in the innovation process. We mention the role of the chairman of Orix, who led the Japanese Association of Directors to promote the appointment of outsiders, but do not analyze his role in greater detail. A promising avenue for future research would be to study the role of institutional entrepreneurs in tailoring foreign models to fit local contexts, creating subfields, and influencing the regulatory authority. This kind of microlevel study would complement the meso (firm) and macro (regulatory) levels of analysis, and would enrich the literature of institutional entrepreneurship (Maguire et al. 2004).

The antecedents of learning from foreign models identified in this study may be neither exhaustive nor relevant to all firms. The identified antecedents—a high level of exposure to foreign capital and product markets, a decline in financial performance, a marginal position in the business community, and a nonmainstream, innovative corporate culture—are based largely on the experience of Sony. We surmise that social, normative pressures may be equally, if not more, important for immediate and late adopters in imitating foreign models. Further studies based on a comparative case-study design (Yin 2003) would help to identify the important factors and the circumstances under which these factors are relevant.

Given our theme of the diffusion of governance innovation, we devote our research effort to studying why and how firms adopted the EOS, but do not compare these firms with those that did not adopt the EOS nor investigate the rate of adoption, which could be a promising avenue for future research. Researchers could study the situational (firm-level) and individual (leadership) factors behind the adoption or rejection of the EOS and the outcome of such action in terms of reputation (domestic and international) and performance. A combination of a comparative case study and a survey study would be highly appropriate for such work.

We believe that our analytical framework is applicable in a number of other contexts, although to different extents for different economies. Economies in Asia and continental Europe have witnessed rising capital market pressures due to the deregulation of their financial markets and an increasing proportion of foreign ownership. In many of these economies, tightly knit business groups that are deeply embedded in insider-oriented culture are dominant (Ghemawat and Khanna 1998, Mahmood and Mitchell 2004). In addition, the state is a pivotal player in such economies, and state-capital relations are negotiable. It is therefore important to examine institutional pressures on governments and their political-economic priorities (Gordon 2004), as well as the responses from domestic firms. For example, in both South Korea and Singapore the government was quick to call for the observation of "global" corporate governance standards after the Asian currency crisis. However, in South Korea most *chaebol* made only superficial adjustments in the face of state demands, and 80% of the outside directors of the *chaebol* boards were still handpicked by the owners of the groups (Larkin 2000). Only a minority of *chaebol* that were on the brink of bankruptcy were willing to adopt more far-reaching corporate governance reforms (Tsui-Auch and Lee 2003). In Singapore, the banking groups that have been strictly regulated by the state have increasingly complied with the Corporate Governance Codes and bowed to the government's call for self-renewal, in part by retiring long-serving, aged directors (Tsui-Auch 2004). However, the Singapore Exchange had to scrap a new Chapter 9B in its Listing Manual which was criticized by companies for giving audit committees overburdensome responsibilities. Also, subsequently developed Best Practice Guide (1998) and Corporate Governance Codes (2001 and 2005) were made voluntary rather than mandatory (Tay et al. 2006). In Germany, many firms announced corporate governance reforms but did not follow them, or implemented them differently to fit their local context (Buck and Shahrim 2005, Fiss and Zajac 2004). Apparently, firms and business groups in these countries, as with their Japanese counterparts, have tailored the Anglo-American model to fit their local context. Certainly, the degree of decoupling in various institutional contexts differs due to differences in the structure of the financial markets, the economy's level of exposure to foreign capital, and the degree of institutional embeddedness. Researchers can validate our framework through single-country studies or cross-national comparative studies of corporate governance innovation. Such studies would aid the development of locally and globally relevant theories that would strengthen the global knowledge base of organization science.

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Appendix. Interview Guide

A. Firm Characteristics
- Has there been any major change in the ownership structure of your company recently?
- Has any significant industrial environmental change exerted impact on corporate governance reforms in your company?
- In your company, has the proportion of foreign sales increased as compared to that of local sales in recent years?

B. Governance Structure Reforms
- Can you confirm that the following corporate governance reform measures that we have documented about your company based on various reports have been implemented?
- When was each measure implemented? Were the measures implemented in different stages?
- Who initiated them?
- How were the measures received among different stakeholder groups in different stages? Did your company experience any internal resistance against such reforms? Were there any contending viewpoints?

C. Motivations and Factors Behind the Reforms
- To what extent was your company satisfied with its previous corporate governance system?
- What were the major factors (internal and external) that triggered your company to undertake the corporate governance reform measures? To what extent did each of the following factors (e.g., rising capital market forces, change in ownership structure, globalization of business operations, rising foreign sales, degree of diversification [product, geographical, etc.], industry factors, decision-making problem at the board level, etc.) shape the reform measures?

• Were there any events or incidents (external or internal) that triggered these proposed measures?

• (Addressed to companies other than Sony) Sony started the EOS in 1997. How did your company perceive its impact on the corporate field? Did your company consider adopting a similar system?

• Was there any social pressure for your company to conform to the governance reform?

• To what extent did the top management influence those reform measures?

D. Field Interactions

• How did the recent statutory changes on corporate governance affect your company's corporate governance structure and practices? Do you think that such changes are desirable?

• Has your company encountered any social pressure (from industrial or professional associations, media, academic and legal communities?) If yes, in what ways?

• Has your company participated in any lobbying activities for or against corporate governance reforms? If yes, how? If no, why not?

E. Organizational Outcomes and Future Direction of Corporate Governance Practices

• With regard to the recent corporate governance reform measures in your company, to what extent is your company satisfied with their implementation?

• Has your company benefited from the reform measures? If yes, in what ways? If no, why not?

• Does your company have any plans to further reform its corporate governance practices? If yes, how? If no, why not?

• Do you think that your company will increasingly adopt the Anglo-American model of corporate governance? If yes, why? If no, why not?

• Or do you think that your company will retain more features from the Japanese governance model? If yes, why? If no, why not?

• Do you think that strong monitoring of top management by the internal corporate governance system (i.e, the board) can improve firm performance?

• Do you think that an outsider-dominated board will bring about benefits for your company or that such a structure is not applicable to your company?

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