Corporate Governance and Mutual versus Stock Ownership: A Case Study of Heisei Life Insurance Crisis

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Abstract
Heisei Life Insurance Crisis was unprecedented phenomenon in the history which dramatically changed the life insurance industry in Japan. Among the 7 bankrupt insurers, 5 were mutual and 2 were stock companies. Now that the oral history of the managers' behavior leading up to the failure is available, it is worthwhile to revisit the issue of corporate governance and mutual versus stock ownership in the Japanese life insurers. By closely reviewing the situation of the 7 insurers as well as one more bankrupt insurer, there will be some limited conclusions drawn as to the views presented in the existing theoretical study which generally affirm the existence of mutual companies and do not see so much significance in making a comparative study between mutual and stock ownership.
Keywords: managers' behavior; oral history; unlisted companies

Introduction

During the 4 years between April 1997 and March 2001, as many as 7 life insurers went bankruptcy in Japan. It is unprecedented phenomenon in the history of insurance industries in Japan and it is called the "Heisei (the era started since 1989) Life Insurance Crisis." Out of 7 insurers, 5 insurers were mutual and 2 insurers were stock companies. Hence you cannot assert that mutual companies are more vulnerable than stock companies if you superficially look at the fact that the stock companies also failed. Although the majority of the 7 insurers were mutual companies, it might not be the case that they failed due to mutual ownership. Rather it might be a natural consequence of the industry situation where mutual ownership has been a prevalent form of life insurers for the past 60 years. However, now that there has been an interesting study made on the cause of the failure of the 7 insurers[1)], it is worthwhile to revisit the issue of corporate governance between mutual and stock ownership based on case study of Heisei Life Insurance Crisis.

The following hypotheses are conceivable:

(1) Because far more number of life insurers were mutual companies, it should be significant that two stock companies experienced the failure. Thus you can draw the conclusion that mutual are not less superior to stock companies with regards to corporate governance. That is to say, the issue of mutual versus stock ownership is not so important as a matter of fact.

(2) As far as corporate governance is concerned, there is no important difference between mutual and stock ownership. This is because there was no effective corporate governance even in the stock companies. While as a matter of theory, stock company is more advantageous than mutual company to get corporate governance properly functioned, you cannot tell one way or another by studying the cases of the failed insurers where corporate governance has been equally intact.

1. Existing Study

(1) Empirical study

There has not been ample empirical study on mutual versus stock ownership in Japan as compared to the US[2)]. This is because the number of life insurers is extremely small in Japan and the most of them have

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been mutual companies for many years. Yanase et al. (2008) is one of them where they made comparison between mutual versus stock, and "keiretsu" affiliation versus non-keiretsu life insurers in Japan and drew the conclusion that mutual and keiretsu companies have less risk taking attitudes than stock and non-keiretsu companies respectively. However the number of stock insurers was only 4 out of total 20 and all 4 stock insurers are much smaller than some mutual companies until 2002[3]. In connection with this study, Kofuji (2010a) proposes another interpretation to the effect that it is due to the scale of company rather than company form and affiliation reasons because mutual and keiretsu companies are far larger than stock and non-keiretsu companies.

(2) Other study

While empirical study has not been so profound in Japan, mutual versus stock ownership has been one of the most important issues for the past 40 years due to very prevalent and unique presence of mutual life insurers in Japan. There has been accumulation of many research papers, articles and theses. Among them there is no strong or one sided view on comparative superiority, efficiency and governance between mutual and stock form (Sugino 2011)

Some of them are as follows.

- While there is some notable tendency that more and more life insurance companies in overseas countries are demutualized recently, I do not see so much significance in demutualization of Japanese companies (Iguchi 2000: 2).
- It is not reasonable that you make comparison between mutual companies and stock companies just from viewpoint of efficiency (Chano 2001).
- It is not very significant to make unilateral comparison between them (Okamura 2006: 226).
- As a result of empirical study in the US, there has been no clear conclusion that either is more efficient than other (Chano 2001).
- There is no evidence that it is a historical certainty that the number of mutual companies will be decreased (Tanaka 2002: 38).
- Whether it is mutual company or stock company is a matter of strategic decision making by management (Yoneyama 2003).
- It is not always true that trend for demutualization is universe. There are many mutual companies in the world who are well run, respected by customers and competitors alike (Birkmaier and Laster 1999: 34).
- Modern nature of mutual company is to prioritize policyholder interest under complete control by manager because expense sharing policy and self-governance by policyholders are no more part of mutualism in the present mutual company in Japan. Therefore what does really matter is manager's ethics and strong leadership to serve for such purposes (Mizushima 1992: 16–7; Mizushima, 2001: 14).
- Because the interests of manager and policyholder do not necessarily coincide, it is up to regulatory development whether mutual company will really pursue policyholder interest (Hetherington 1969: 1102–3). In Japan, on the contrary, what actually precluded mutual companies from achieving policyholder interest in 1980s was government policy to protect the industry as a whole (Mizushima, 2001: 10–3).
- As for corporate governance of mutual company, Japan might be ahead than UK in that some measures are incorporated to make its governance system comparable to stock company and that the procedures of councils meeting and policyholders meeting have been built in the system (Hisamatsu 2006: 70).

2. Heisei Life Insurance Crisis

(1) The magnitude of the crisis

It was called as crisis because the number of 7 was large enough as compared to the total number of life insurers of 31 and all 7 insurers were middle market and long lived companies. As of 1996, the total number of life insurers was 31, out of which 20 insurers were traditional companies with 16 being mutual and 4 being stock form. Hence the life insurance industry in Japan was called 20-company system for 50 years after the war (See Table 1). The total assets of the 7 insurers exceeded 10% of the assets of the entire industry and some 7 billion yen was poured from the life insurers guarantee fund.

The crisis has changed the landscape of the life insurance industry together with the reform brought by the sweeping revision of the Insurance Business Law which was enacted in 1995 and put into force in 1996. In 1996, immediately before Nissan went bankruptcy, there were 20 traditional insurers which were dominant in terms of amount of premium, This was the situation which had lasted for nearly 50 years after the war (World War II). That was the so called "20-Company system." The crisis greatly shook this system. The number of traditional insurers reduced significantly and instead the number of foreign insurers dramatically

Table 1. 20-Company System in 1996[a)]

	Company Name	Form	Premium Income (billion yen)	At present/successor
1	Nippon	mutual	¥5,893	mutual
2	Dai-ichi	mutual	¥3,884	stock (2010)
3	Sumitomo	mutual	¥3,428	mutual
4	Meiji	mutual	¥2,519	merged (mutual)
5	Asahi	mutual	¥1,713	mutual
6	Mitsui	mutual	¥1,586	stock (2004)
7	Yasuda	mutual	¥1,501	merged (mutual)
8	Taiyo	mutual	¥1,281	stock (2003)
9	Daido	mutual	¥1,105	stock (2002)
10	Chiyoda	mutual	¥860	AIG
11	Fukoku	mutual	¥858	mutual
12	Kyoei	stock	¥814	Prudential(US)
13	Nippon Dantai	stock	¥670	AXA (2001)
14	Toho	mutual	¥598	GE Edison
15	Daihyaku	mutual	¥500	Manulife
16	Nissan	mutual	¥225	Aoba
17	Tokyo	mutual	¥211	Taiyo/Daido
18	Heiwa	stock	¥84	Foreign company
19	Yamato	mutual	¥56	stock (2002)
20	Taisho	stock	¥48	Azami
20 companies total			¥27,834 (95%)	
Others: 24 companies[b)]			¥1,520 (5%)	
Total: 44 companies			¥29,354	

Source: Prepared by the author based on the *Seimei-Hoken Tokei Go* (Statistics of Life Insurance Business in Japan) 1997.
a) This is the year where you can see the industry picture before the crisis and the reform of Insurance Business Law started to change it dramatically.
b) Thirteen companies newly entered the market in October, 1996.

increased. Furthermore as a result of revised Insurance Business Law, 11 new life insurers were founded in 1996. All foreign insurers and newly established insurer were stock ownership. Hence the presence of mutual company has not been so prevalent as in the past 50 years. In 1980 the number of mutual insurers was reduced from 16 to 6 and percentage of premium was reduced from 95% in 1980 to 48% in 2010 (see Tables 2 and 3). The landscape after the crisis is shown in the Tables 4 and 5.

The numbers in Table 3 were obtained from *Seimei-Hoken Kyokai Hyakunen-Shi* (One hundred years history of Life Insurance Association) and *Nissei-Kisoken* (NLI Research Institute) *REPORT*. In 1908, there were 35 life insurance companies including ones under liquidation process and having stopped business. The numbers shown here are the ones of the companies who were members of the Life Insurance Companies Association which was established in 1908. The three foreign companies in 1980 were American Life Insurance Company, American Family Life Assurance Company of Columbus and Seibu Allstate Insurance Company. The

Table 2 Dominance by Mutual Companies

	Percentage of Mutual Cos. by Premium	Number of Mutual Companies
1980	95%	16
1997	89%	15
2000	85%	11
2010	48%	5

Source: Data of 1997 was obtained from Birkmaier and Laster (1999, p. 18) and data of other years from *Seimei-Hoken Tokei Go* for the years.

Table 3. Number of Life Insurance Companies by Year and Type

Type / Year	(A)		(B)	(C)	(D)
	Mutual	Stock			
1908	1	15			
1950	16	4			
1980	16	4	3		
2000	11	1	15	13	3
2010	6	7	18	9	6

Source: See the description in the main text.

Table 4. Proportion of Premium Income by Company Type (2002)

	Number	Premium (Trillion yen)	Increase (%)	Share (%)
(A)	11	19.70	△ 7.8	76.2
(B)	18	4.58	29.0	17.7
(C)	10	0.97	38.2	3.8
(D)	2	0.61	△ 5.4	2.4
Total	41	25.86	△ 1.6	100

Source: *Nissei-Kisoken REPORT,* September 2003.

Table 5. Proportion of Premium Income by Company Type (2010)

	Number	Premium (Trillion yen)	Increase (%)	Share (%)
(A)	13	19.03	1.1	68.6
(B)	18	6.18	△ 0.4	22.3
(C)	9	1.63	△ 9.3	5.9
(D)	6	0.92	9	3.3
Total	46	27.76	0.3	100

Source: *Nissei-Kisoken REPORT*, September 2011.

four traditional stock companies in 1980 were Heiwa, Taisho, Nihon-Dantai, Kyoei out of which Heiwa merged with foreign company, Taisho and Kyoei went bankruptcy. In 2001, Nihon-Dantai merged with AXA Group making the number of traditional stock company zero. Among 7 traditional stock companies in 2010, 4 are T & D Financial, Dai-ichi Frontier, Fukoku Shinrai, and Medikea which were founded by parent traditional companies in recent years. Six category (D) companies in 2010 are Sony, Orix, Airio, Life-net, Midori, and Nextia (*Nissei-Kisoken REPORT* September 2011). Life-net, Airio Life and Midori-Life started operations in 2008 and Nextia Life is a new name of SBI-AXA from 2010. Life-net is the company founded independently without having any sponsor companies for the first time in 74 years (Iwase 2009: 18).

(2) Environmental difficulties

Following the high degree of economic growth in the 1960s and 1970s, there was a so called "bubble economy" in the late 1980s. As measures to the extremely favorable balance of trade and large amount of capital inflow to the US due to its high interest rate, there was a Plaza accord where the policy to introduce the exchange rate in favor of yen was agreed upon among the G5 countries. In addition to the shift to strong yen, Japan took drastic monetary policy for easing to boost domestic economy. This was because there was the opinion promulgated that the strong yen would not only curtail trade but also dampen the domestic economy. Between January 1986 and February 1987, the official discount rate was reduced 5 times from 5% to 2.5%. The government took the action to increase domestic consumption, investment into public enterprise and to expedite construction of houses and urban redevelopment. However, in spite of the strong yen, favorable balance of trade continued resulting in over easing of money. The government enacted the Comprehensive Resort Improvement Act in 1987 to encourage investment which would not cause trade friction. This brought about the real estate bubble. The Ministry of Finance (MOF) prohibited the real estate loan in March 1990. In October 1990, the Nikkei Stock average plunged to about ¥20,000 from the peak of ¥38,915 in December 1989, which represented the burst of bubble economy. Since then, Japan had been in recession with low stock value and interest rate for 20 years. The low interest rate and the depreciation of the stock value were two of the most important causes of the failure.

Along with the economic growth, life insurance industry also developed to be one of the largest in the world. More than 90% of the household contracted life insurance although it was the second largest spending after house expenses with the average amount of yearly premium being ¥450,000 per family (Iwase 2009: 33). It was sold well as a security for inadvertent loss of a bread earner in the family. Therefore one of the most major products was long term life insurance which contributed very much to the rapid growth of life insurance in Japan. In 1980s, pursuing and competing with others for expansion of the scale, the life insurers changed their strategy so as to sell savings type insurance such as endowment insurance and endowment insurance with term insurance as a policy rider. The savings type insurance was very much in line with the Japanese consumer's taste that would prefer savings type insurance to pure term insurance. Those savings type insurance was sold with high guaranteed interest rate and high dividend. It was because the interest rate was high during those years and insurers competed to offer high dividend. The gap between the actual interest rate and the guaranteed interest rate was the back spread which intrigued the life insurers for many years up to the present.

As of March 2000, the assumed interest rate of top 14 insurers was 3% to 4% and the actual interest rate was 2% resulting in the back spread of ¥1.6 trillion (Fukao and JCER 2000: 5). In case of large insurers, they had mortality rate profit and expense rate profit to make up the loss of back spread. However, the majority of medium and small size insurers had no alternative but to cover the loss by profit on securities sold. Then, the lowering of the stock value had the adverse effects in the two fold. One, they could not gain such profit anymore. Two, their assets deteriorated by the depreciation of the value. By the way, during the economic growth where the stock price hiked in the long run, latent profit on securities in balance was the buffer for inadvertent loss for all companies not just life insurers.

Thus low interest rate and low stock value as a result of bursting bubble economy, change of product strategy and competition for expansion of assets, high guaranteed interest rate and high dividend are all environmental difficulties to which all life insurers were commonly exposed in the crisis.

3. Company Profile and Cause of Failure

As for Heisei Life Insurance Crisis, there have been many books and articles published on its background, mechanism, cause, outcome and ramifications etc. Some of the representatives are Fukao and JCER (2000, 2002), Kofuji (1999, 2001, 2003), Takeda (2008) and Uemura (1999, 2000, 2008). References were made to those books and especially in connection with description of businesses as well as facts and anecdotes surrounding the management of the companies, Uemura (2008: 82–194) were relied upon, which is the book written based on the oral history[4)] taken from 33 persons who were actually involved and witnessed the crisis leading up to the bankruptcy as insiders of the companies.

(1) Nissan Life Insurance Mutual Company

Nissan was founded as a company belonging to Hitachi and Nissan group in 1909 and depended on group business until the former 1980s. At Nissan, the proportion of group insurance was larger than personal insurance. This is rather unique in the industry and, there were only 2 such companies. They were Nihon Dantai and Tokyo. Some 70% of Nissan' group insurance was from the Hitachi and Nissan group (Uemura 2008: 88). Towards 80th anniversary of the company in 1989, they decided to aggressively pursue the long time goal to develop and expand into personal insurance market. Because it was difficult for them to cope up with large insurers regarding the business model of using sales persons, they chose to form alliance with banks and to sell non-installment personal pension insurance with high interest rate and high dividend. They devised the personal pension insurance whose premium would be paid by the loan from banks. The number of banks with whom Nissan tied up was over 160 throughout the country (Takeda 2008: 8). They were just eager to enlarge their business and to lessen their expense loss without realizing risk of high interest and high dividend and reliance upon the particular product.

The personal pension insurance with the loaned premium sold very well and the premium was 235% in 1987 and 219% in 1988 of the previous years. The assets increased from ¥368 billion to ¥1.6 trillion during 1985 and 1989. Nissan generated the premium of 1.4 trillion for the three years from 1987 to 1989, nearly 60% of which (¥800 billion) was personal pension insurance. Out of which, ¥730 billion was non-installment insurance with assumed interest rate of 5.5% to 6% and term of 20–30 years. The proportion of personal pension to the technical provisions was 56% as against the industry average of 7% (Uemura 2008: 91–2).

In order to pay such high interest and dividend, they made investment into volatile stock and foreign bond and were heavily influenced by change of stock price and exchange rate of foreign currency. The investment balance of the stock became 300% for 3 years from 1986. As of 1991, they summed up loss due to devaluation of the stock and recouped the deficit from the technical provision and capital gain from the real estate. While the profit from three sources was ¥30 billion, the depreciation loss of the stock was ¥90.3 billion (Uemura 2008: 94). As a result, the ordinary profit was 1/30 of the previous year. From 1993, Nissan could not achieve profit of three sources any more owing to back spread of interest rate and given the latent loss of assets, they were in the condition of deficiency. Besides them, as a measure in closing accounts, Nissan came to invest into structured bond and derivatives which aggravated their performance due to the change of market condition (Takeda 2008: 8–9). Thus Nissan was as a matter of fact insolvency as early as 1994.

Mr. Sakamoto was the president from 1987 through 1994. He was the vice president in 1981 and had taken initiative in preparing the middle term management plan in 1985. At Nissan, the sales department had power but Mr. Sakamoto had no experience in sales. Mr. Sakamoto together with his 4 or 5 aides had influential power. Mr. Sakamoto did not exert any leadership to improve the situation (Uemura 2008: 97). He was simply pleased with the sales promotion by alliance with banks. They were not concerned about the risk of interest rate and only interested in movement of stock price. The relationship between the financial department and the actuarial department was not good. Thus Nissan did not have asset-liability management (ALM) (Uemura 2008: 98).

About 60% of the representative meeting was Hitachi and Nissan group people and no check and control by the meeting (Uemura 2008: 99–100). Eight companies from Hitachi and Nissan group had sent the directors but they did nothing in the board meeting with the exception of Nissan Fire. MOF did notice the problem in the early 1990s at the time of audit. However the audit then was to review the assets and profit from three sources for each year. So it is questionable whether MOF had sensed any problem in interest risk in connection with the growing technical reserves (Uemura 2008: 101). Although Nissan was almost insolvent around 1994, MOF did not take any decisive action until 1997. The reason for that was probably because no viable system and plan was prepared yet for rescuing the insolvent insurer (Uemura 2008: 101).

(2) Toho Life Insurance Mutual Company

Toho was founded as the first draft insurance company in Japan in 1898 and Mr. Seizo Ota became the president in 1909 since then Ota family controlled the company. In the late 1980s, Toho headed towards enlargement of their business and aggressively sold savings type insurance. As a result, the assets have grown to be 280% from 1985 to 1989 (Uemura 2008: 103). In order to pay high yielding interest, Toho has come to make investment into high risk structured bond. Besides the growth of assets, it was Toho's aim to eliminate expense loss and pay policyholder dividend as high as large insurance companies. In 1989, Toho achieved the high dividend but would have to suffer from heavy burden of high yielding interest rate as well as expensive value of stock.

Mr. Ota who became the president in 1977, was a unique person as a manager of insurance company (Uemura 2008: 106–8). He was eager to rescue other defunct company, making investment into speculative stock etc. without paying due diligence and interest to the management of the insurance company. He was rather insistent upon the personnel matter and fired the capable member of the management leaving only yesman around him. The aides surrounding Mr. Ota made inappropriate and unethical behavior using the company assets. Directors were often chosen from the sales department and they did not have enough understanding about the company management.

Toho increased the stock investment during the bubble economy and the depreciation loss of the stock was ¥162.2 billion being 20% of the total stock value in 1991 (Uemura 2008: 110). Toho experienced the first loss of insurance business in 1993. The latent profit of the stock, which was ¥390 billion in 1989, dwindled to ¥16 billion. MOF audited and pointed out the problems but the management did not take proper action. Latent loss of the stock was ¥70 billion as of May 1993. Around 1993, younger group of the management took initiative of management reform (Uemura 2008: 112). They determined that recovery on their own was not easy and probed for alliance strategy. Toho finally reached the agreement with GE Capital to the effect that they will jointly establish GE Edison Life Insurance so as to have the company purchase the sales channel and that Toho would manage the maintenance of the past contract only in 1998 (Takeda 2008: 11). While Toho received ¥120 billion as goodwill expenses etc. it was a disadvantageous deal for Toho (Uemura 2008: 114).

In June 1999, Toho went bankruptcy when Tohmatsu requested the disposition of latent loss and bad debt in the amount of ¥231.3 billion, which resulted in the deficiency of ¥200 billion (Fukao 2000: 114). Under Mr. Ota, there was no internal control and no risk management. One of the aides did not produce the breakdown of the investment for the meetings of the managing directors in the late 1980s and did not provide with the actuary department any data for solvency margin in 1990s (Uemura 2008: 115). A member of the representative meeting was chosen by the presidents as he liked (Uemura 2008: 116). MOF had requested the president's resignation in 1993 and Mr. Ota resigned in 1995.

(3) Daihyaku Life Insurance Mutual Company

Daihyaku was founded as one of the Kawasaki group company in 1914. Their main product was savings type insurance from the beginning. Although they tried to develop their business into life insurance section for long time, the proportion of savings insurance to the personal insurance was still very high, that is to say, 73% in 1980 and 60% in 1985 (Uemura 2008: 121). As a result, their profitability was low and Life Insurance Association adopted their performance data as bench mark to determine the mortality rate, expense loading and dividend rate until 1980s (Uemura 2008: 121–2). Daihyaku could not overcome the problem of expense deficit and insufficient mortality rate profit due to their portfolio where the weight of small, savings insurance was very high. This is contrasted with Taiyo which had similar portfolio and succeeded in improving the performance by drastic reform of sales, product innovation and cost cut (Uemura 2008: 123–4).

The above problem has emerged in 1990s when they could not obtain higher investment return. Back spread occurred in 1992, interest rate loss could not be made up by expense rate profit and mortality rate profit in 1993. In 1994, Daihyaku experienced ordinary loss for the first time. The financial department issued the warning, but the management did not have sense of any crisis. From 1997, they launched middle term management plan and obtained the fund of ¥19 billion from 4 banks. After the failure of Nissan and Toho etc., cancellation rate increased from 13.3% to 19.1% in 1997 (Uemura 2008: 126). Daihyaku contracted financial reinsurance with RGA and received the commission of ¥10 billion which was put into the technical reserve. Furthermore, Daihyaku issued the subordinated debenture of ¥38 billion to West German Bank , which was later found to be improper (Uemura 2008: 126; Takeda 2008: 13).

The proportion of stock to the assets was 23% around 1990. Daido reduced the weight from 20% to 10% between 1992 and 1993. On the contrary, Daihyaku was delayed in disposing of stocks partly because Kawasaki family did not like to do it and sales department had stronger power within the company (Uemura 2008: 127).

In 1994, Mr. Shinjiro Kawasaki became the president but they determined that they had no alternative but to make alliance with other company (Uemura 2008: 128). It was their consideration that the only viable way for mutual company to obtain fund was the scheme of Toho, that is to say, separation of new and old business. They decided on a plan similar to Toho that they would receive ¥80 billion by selling the products, sales offices including sales person to Manulife Financial and that they would continue to operate as a maintenance company of old business only (Takeda 2008: 13). Immediately after the alliance, there was sudden increase of cancellation which was an influence of Toho bankruptcy and loss of tens billion yen due to foreign security investment. In 1999, Financial Control Agency (FCA) requested to review due diligence of assets. In 2000, FCA issued Operation Improvement Order in connection with the above subordinated debenture. The top management did not know about this subordinated debenture and only Mr. Shinjiro Kawasaki, then director of investment, and his subordinate were aware of it according to the newspaper (Uemura 2008: 129). After this FCA order, cancellation further increased resulting in insolvency and FCA ordered stop doing business.

While Daihyaku did not treat actuary lightly, actuarial opinion was not reflected on the management strategy (Uemura 2008: 132). There was no communication between the financial and actuarial department. In 1990s, they formed ALM committee but they did not understand what to do (Uemura 2008: 133). The representative meeting was just ceremony (Uemura 2008: 133). There was no governance by MOF. There were several presidents from other than Kawasaki family, but they did not exert strong leadership (Uemura 2008: 131). The management was always under influence of Kawasaki family.

(4) Taisho Life Insurance Co., Ltd.

Taisho was founded in 1913 and their main products were savings type insurance such as endowment insurance by sales persons. As a traditional company, it was one of the smallest and the assets at the peak time

(1996) was ¥238 billion which was only 0.6% of Nippon Life. Although it was small, Taisho was doing business steadfastly until when Nissan failed in 1997 resulting in increase of cancellation and back spread deteriorated their financial performance.

In August 1999, FCA audited and found out the excess liability of ¥4.3 billion and early warning measures were taken in February 2000. Taisho made allocation of ¥4.5 billion new shares to Claremont Capital in return for making investment into ¥100 billion into foreign security. The president of Claremont was arrested for fraud of ¥85 billion in August and Taisho was ordered to halt business by FCA.

The insurance administrator having looked into the matter concluded that the reasons for the failure are as follows. Taisho sold savings type insurance with higher interest rate (average 4.05%) than other companies. Under insufficient internal control, amount of bad debt significantly increased. Regarding several important matters, directors and auditors did not perform their duties. As of 1999, the solvency margin dropped to 67.7% due to back spread and investment loss. The last resort for Taisho was to increase capital by issuing new shares to third party. However the third party who received the new shares was not conventional financial institutions but the Claremont Capital Holdings Co. Ltd, and its president in person only, which turned out to be a problem as stated above.

In 2001, Yamato Life Insurance Mutual Company and Softbank Finance Co. Ltd. jointly founded Azami Life Insurance Co. Ltd. The portfolio of Taisho was transferred to Azami for ¥7 billion in 2001. Azami also received the goodwill from Yamato Mutual which remained as a maintenance company. In 2002, Azami and Yamoto Mutual merged making Yamato Life Insurance Co. Ltd. Yamato Life Insurance Co. Ltd. went bankruptcy in 2008. It was because they suffered investment loss on their high risk investment as a result of the World Credit Risk.

(5) Chiyoda Life Insurance Mutual Company

Chiyoda was established in 1904 and was the second mutual company in Japan. The first president was Mr. Ikunoshin Kadono of Keio University. It was ranked No. 2 in terms of insurance in force in 1924. It sold the first group term insurance in 1948 and the first group pension insurance in 1950, the first group credit life insurance in 1961. They formed "Satsuki" group with Chiyoda Fire, Tokai Bank, Chuo Trust Bank, and Tomen in 1970. Before the war, Chiyoda was one of the "Big 5" companies.

However Chiyoda was delayed in shifting their sales force from agency (Keio network) in the country to sales person in cities and product from endowment insurance to endowment insurance with term insurance as a policy holder (Uemura 2008: 136). Then the ranking dropped to No. 10 or so. In 1982, Mr. Kanzaki became the president and advocated "return to big" as a company's goal. Their emphasis was to sell savings type insurance and especially group pension insurance. They were historically strong in group insurance. As for personal insurance, they sold a lot of non-installment endowment insurance and the proportion of non-installment premium was 40% with the industry average being 25% in 1989 (Uemura 2008: 138). They grew to be ranked No. 8 and were referred as "Big 8."

The investment department of Chiyoda was well known for its very conservative investment policy. In the 1980s, however, it became their mission to cooperate to sales department. That is to say, they provided loans to corporate client in return for selling insurance. As a result of having bought stocks at the request of the sales department, the stock balance at the end of 1989 became 300% of 1986 (Uemura 2008: 136). From the end of 1997, the depreciation loss of the stock amounted over ¥100 billion (Uemura 2008: 136).

In the course of selling a lot of savings type insurance with high interest and high dividend in the late 1980s, Chiyoda inclined to make high risk investment such as loan to real estate companies and non-bank companies, stock, specified money in trust etc. some of them are Yokoi group (loan balance ¥80 billion), Aichi group (¥80 billion), Matsumoto Yu Shoji (¥37 billion) etc. which loans were executed during 1988 and 1990 (Uemura 2008: 139). The investment and loan leading up to bad debt was done by one of aides of Mr.Kanzaki. He had no prior experience of finance but given exclusive power on financial matters. As of March 1993, bad debt amounted to ¥550 billion being 20% of all loans (Uemura 2008: 136).

In June 1993, top 8 life insurers made the amount of bad debt public for the first time (Uemura 2008: 144). The amount of Chiyoda was ¥231.6 billion which was extremely large compared to ¥36.7 billion of Sumitomo whose investment policy was famous as aggressive. The actual amount of debt was some ¥400 billion. In 1995, equity capital was minus ¥236 billion. In spite of the critical situation, the management did not take any quick and decisive action. Compared to other failed insurers, Chiyoda still generated expense rate profit and mortality rate profit and so the total of three sources of profit was positive. In 1994, thanks to lowering of guaranteed interest rate of group pension insurance from 4.5% to 2.5%, the profit of 1996 increased from ¥ 22.9 billion to ¥72.4 billion. In mid 1990s, disposition of policy stock was discussed because the latent profit of the stock amounted over ¥200 billion. However, there was a very strong objection from Mr. Kanzaki group and the sales department, they could not make any decision to sell the stock.

Chiyoda acquired the fund of ¥50 billion, the subordinated loan of ¥77.5 billion from Tokai Bank etc. and disposed of the bad debt of ¥138.9 billion in the mid 1990s. However the cancellation continued to increase and the group pension insurance in force decreased from ¥3 trillion at the peak to ¥1.2 trillion in 1998 (Uemura 2008: 149). In the later 1999, stock market plunged and Chiyoda started to negotiated with the foreign investors in vain. Because the banks turned down to cooperate, the alliance with the foreign insurers ended unfruitful. In October 2000, Chiyoda applied for bankruptcy with the Tokyo District Court.

Actuary group was part of planning department and they were not respected within Chiyoda (Uemura 2008: 152–3). They had no power against the sales department. There was no ALM and no governance by MOF (Uemura 2008: 153–6).

(6) Kyoei Life Insurance Co., Ltd.

Kyoei was founded as a reinsurance company in 1935 by Mr. Saburo Kawai who was a famous actuary having once served as chairman of Actuary Association in Japan. After the war, it started as a life insurance company. Kyoei was not a member of any business group and did not have any given customer bases. So, it developed the niche market such as teachers and educational institutions and Defense Agency employees.

Kyoei mainly sold term insurance instead of endowment insurance which was a major product of the industry at that time until the late 1980s. Kyoei was the first who sold endowment insurance with term insurance as a policy rider in the 1960s and personal pension insurance in 1963. As for personal insurance in force, Kyoei was 10th in1970s and 8th 1980s. It sold savings type insurance through allied group with guaranteed interest rate of 3.75%. Kyoei was in the upper group of ranking in terms of insurance in force but in the lower group with regards to assets. So Kyoei changed the strategy so as to sell non-installment endowment insurance with the interest rate of 5.5% in 1987. It was limited to the term of 10 years (Uemura 2008: 158–60).

What made the problem of back spread serious was not only that the term of their endowment insurance was 10 years but that Kyoei continued to sell the insurance after other insurers halted to do that. After 1991, the increase of the assets of the industry was 8.8% in 1991, 8.9% in 1992, 8.4% in 1993, and that of Kyoei were 12.3%, 13.9%, 13.0% respectively (Uemura 2008: 161). One of the reasons for the delay was that customers were employees of the tied up group and another was that there was no one who could to that in spite of the objections of the sales department. For several years before the failure, the situation continued such that interest rate loss was ¥100 billion, mortality rate profit was ¥65 billion, expense rate profit was ¥20 billion and that the deficit was ¥15 billion. In addition to the back spread, the loss on securities sold was ¥18.5 billion in 1996, ¥47.7 billion in 1997, ¥52.3 billion in 1998, and ¥90.8 billion in 1999 (Uemura 2008: 164).

While Kyoei negotiated to enter into a partnership with the Prudential, it was not fruitful because the stock market did not improve as expected and Kyoei lost ¥30 billion being the fund provided to Dai-ichi Fire as a result of its bankruptcy in March 2000 (Uemura 2008: 167). Mr. Kawai was the president from 1935 to 1971 and there were three presidents after him but all of them were under the influence of Mr. Kawai who was the only dictator until his death of 1998. Mr. Kawai was different than before in 1980s for his age and he resigned from the director in 1992. Nevertheless the top management totally relied upon Mr. Kawai. So the management was done by Mr. Kawai and his two aides until the end (Uemura 2008: 168–9). Kyoei was an unlisted stock company and the board meeting was only the ceremony. There was no governance from MOF (Uemura 2008: 172).

(7) Tokyo Life Insurance Mutual Company

Tokyo was founded in 1895 as a religion group life insurer in Kyoto and became a Nomura group company in 1934. It restarted as Tokyo Life mutual company in 1947. Tokyo was one of 4 zaibatsu companies following 5 big companies before the war. While Tokyo was as big as Fukoku and Daido in mid 1960s, it dwindled to half of Fukoku and one third of Daido in late 1970s (Uemura 2008: 175). Because their dividend was smaller than large companies, they were losing policyholders from the work place market. The sales persons depended upon family and community ties to sell insurance resulting in higher rate of turnover. Compared to the size of the company, they paid larger cancellation dividend for which they relied on profit on securities sold. Under the circumstances, profit on the expense ratio was lower than other insurers.

Tokyo set out for an aggressive sale of personal pension insurance by loaned premium in mid 1980s and it doubled the assets from 1987 to 1989. The guaranteed interest rate was 5.5% to 6.25%. After 1990 when loan interest rate hiked resulting in the reduction of personal pension insurance, it began to sell group pension insurance with high interest rate. Group pension insurance in force expanded from ¥230 billion in 1989 to ¥500 billion in 1993, in spite of the fact that they had a problem of the back spread in 1992. In late 1980s, it summed up profit of ¥20 billion on securities sold to cover high cost dividend obligation. However they were cross deal, the value of stock balance went up year by year (Uemura 2008: 176–9).

The management spent great amount of money to build office building and system investment without taking into consideration that the assets are really obligation. In 1992, the problem of back spread surfaced for the first time but the management did not take any decisive measure regarding it passing problem. They could not make up the loss due to back spread with expense profit and mortality profit anymore and the ordinary profit became negative in 1994 (Uemura 2008: 181). The failure came as if it had been a natural death due to no management or inappropriate management over the long time. That is to say, the reasons for failure are low profit profile, sudden increase of assets and inadequate investment into stock, foreign currency security and structured security. Furthermore, there were misconduct and illegal behavior by top management in the early 1990s. After finally having realized the serious problem, Tokyo tried to demutualize and form alliance with foreign company in vain leading up to the failure in March 2001.

Mr. Shibayama was the president from 1977 to 1986. He was the director in 1957 and the representative director in 1969. Mr. Shibayama was only enthusiastic about sales promotion (Uemura 2008: 187–8). His successors were also from the sales department. At Tokyo, the sales department had power and the presidents who only had the experience of sales did not very well understand the figures of the management. The top management was not serious enough to improve the situation of the crisis. Although they started the ALM strategy board so as to introduce Enterprise Risk Management in 1996, what they actually did was mainly the due diligence of the loan and they were not concerned about the market risk and interest rate risk (Uemura 2008: 190). Tokyo was very close with the Daiwa Bank who tried to support Tokyo but could not avoid the failure.

4. Implications of Study

(1) 20-Company system

The 20-Company system consists of 16 mutual and 4 stock companies (See Table 1). Out of 16 mutual companies, 5 mutual companies, and out of 4 stock companies, 2 stock companies failed. Thus the failure rate is 5/16 (31%) for mutual and 2/4 (50%) for stock ownership. Thus stock ownership is more vulnerable. This is not fair because larger corporations are all mutual companies with all stock companies being small. Then what about the ratio if you take into account only the middle market mutual companies. The top 7 companies are "large" and the middle 10 companies are "middle" with the remaining 3 (Heiwa, Yamato, Taisho) being "small." Then as for 13 medium and small companies, the ratio is 5/8 (63%) for mutual and 2/5 (60%) for stock companies. So the failure rate is not much different between mutual and stock ownership. However does analysis of this type make sense? We need to take a look at 4 stock companies.

(2) 4 stock companies

Four stock companies were all unlisted companies. As for their size, please see Table 1 and Table 6. None of them exists any more. That is to say, no traditional insurer of stock ownership has survived to the present. Two went bankruptcy. Other two were merged by foreign insurers. Nihon Dantai and Heiwa.

As you will see from the profit in the Table 6, both are considered to be rescue type merger. It might be said that the two could avoid bankruptcy because they were stock companies and therefore merger was easier than bankrupt mutual companies. But it is probable that the foreign insurers merged with them for the reasons that they had attractive sales channel etc. So, it cannot be substantiated that as a stock company, they had better corporate governance than other two mutual companies.

(3) 5 mutual vs. 2 stock companies

All 7 insurers are medium and small size companies. So, the size of company had something to do with the failure. Six insurers were very traditional companies with the history of 87 to 107 years except that Kyoei had the relatively shorter history of 66 years. Other than that, 7 insurers are well spread or balanced regarding size, lines of business and origin/ownership etc. (See Table 7). Besides the mutual v. stock ownership, what was likely to have some relationships with

Table 6. Profile of 4 Traditional Insurers of Stock Ownership under 20-Company System

	Assets	Profit	Employees	Shareholders
Kyoei	¥5436 B	¥200 M	3037 (+16597)	not available
Nihon Dantai	¥385 B	¥2 M	2807 (+6480)	322
Heiwa	¥587 B	¥133 M	817 (+2344)	283
Taisho	¥225 B	¥37 M	393 (+10919)	not available

Source: Prepared by the author based on *NIKKEI*; Annual Corporation Reports (UNLISTED) 1996.
B, billion; M, million. Employees & Shareholders are number of persons or entities, numbers of employees within the parenthesis are sales persons, data as of 1996.

Table 7. Demography of 7 Insurers

Company	History	Form	Size	Lines	Group
Nissan (16)	1909–1997 (89)	mutual	M	C	G (Hitachi-Nissan)
Toho (14)	1898–1999 (102)	mutual	M	P	F (Ota family)
Daihyaku (15)	1914–2000 (87)	mutual	M	P	G (Kawasaki)
Taisho (20)	1913–2000 (88)	stock	S	P	Independent
Chiyoda (10)	1904–2000 (97)	mutual	L	C	G (Satsuki)
Kyoei (12)	1935–2000 (66)	stock	L	C	I (Founder)
Tokyo (17)	1895–2001 (107)	mutual	M	P	G (Nomura)

Source: Prepared by the author based on Uemura (2008) etc. The parenthesis after company name is ranking by income in 1996 (see Table 1).
L, large; M, medium; S, small. The size is the comparison within 7 insurers. C, commercial line; P, personal line; G, group company; F, family company.

governance structure was the origin/ownership. In this connection, 4 insurers belonged to a large business group and one was controlled by the family with another being dominated by the founder. Even among the 4 insurers belonging to a group, there were the dictators. They were Mr. Sakomoto of Nissan, Mr. Kawasaki of Daihyaku, Mr. Kanzaki of Chiyoda, Mr. Shibayama of Tokyo, making the significant feature that 6 companies had the dictators who served as the president and chairman for a long time (See Table 8). While 7 insurers varied in several ways, there was one important fact common to most of them. That is to say, they had one man who had the power for long time and either that man had no ability to manage the company or after that man, no successor could properly manage the company. There was no evidence that the difference between mutual versus stock ownership had somehow influenced the failure or outcome of the failure. Mutual versus stock ownership was just one of several diversifications with the overwhelming fact that there was no management in the company.

(4) Yamato Life Insurance Co., Ltd.
There was one more insurer which went to bankruptcy in 2008. It was Yamato Life Insurance Co. Ltd. Yamato's case is not included in the Heisei Life Insurance Crisis because it took place after the crisis was over and under the world credit crisis due to Lehman shock. The reason for the failure was their investment inclined to high risk securities (Kofuji 2010b). At Yamato, the average assumed interest rate was 3.35%. Their investment was public and corporate bond (18.1%), stock (14.6%), foreign securities (23.9%), loan (9.6%) in 2007, whereas they were 37.3%, 7.4%, 12.1%, 20.8% in 2002. This shows that the investment shifted from public and corporate bond and loan to more risky stock and foreign securities. The stock and foreign securities increased from7.4% to14.6% and from 12.1% to 23.9% respectively. On the contrary, the public and corporate bond and loan reduced from 37.3% to 18.1% and from 20.8% to 9.6% respectively.

Yamato was a company with a rather strange history. Yamato was one of 20 traditional insurers. It was a

Table 8. Managers' Behavior and Corporate Governance.

Company	Managers' behavior and corporate governance
Nissan (mutual)	Mr. Sakamoto 1987–1994, 8 years (vice president from 1981) No care about interest risk and no leadership 4 or 5 aides given too much power Representative meeting consisted of affiliated group's employees MOF possibly aware of insolvency situation around 1994 and no action
Toho (mutual)	Mr. Ota 1977–1995, 19 years, no interest in managing insurance company, occupied by strange idea other than insurance Too much power given to aides, confidentiality system
Daihyaku (mutual)	Mr. Daijiro Kawasaki 1965–1973 (1987), 23 years, Mr. Mr. Fukuchi 1987– 1996, Mr. Komori 1996–1998, no leadership Mr. Shinjiro Kawasaki 1998– (son of Daijiro) Representative meeting was just ceremony
Taisho (stock)	Directors and auditors did not perform their duties on several important matters.
Chiyoda (mutual)	Mr. Kanzaki president/chairman 1982–1999, 18 years, no experience other than sales, did not do anything by himself 3 aides were given too much power One aide in charge of finance was wrong selection, he did not have any experience of finance
Kyoei (stock)	Founded by Mr. Kawai (actuary) Mr. Kawai was dictator from 1935 through 1998 until his death Mr. Tayama (1986–1994), Mr. Otsuka (1994–2000) totally depended on Mr. Kawai who did not have energy and capability he had before in 1980s, that is to say, no management after Mr. Kawai in 1980s
Tokyo (mutual)	Mr. Shibayama 1977–1986 (1957 director and 1969 managing director), and his successors were from sales only background, did not well understand management Inappropriate behavior by Mr. Shibayama and another director No management

Source: Prepared by the author based on Uemura (2008) etc.

mutual company as small as Taisho, although Taisho was a stock company (See Table 1). The predecessor company of Yamato was founded as a draft insurance company in 1911. It converted to Yamato Life Insurance Co. Ltd in 1945 and restarted as Yamato Life Mutual Company in 1947. Yamato was restructured into two companies with one being Yamato (old) which only dealt with old businesses and another being Azami which was founded jointly with Softbank Finance to succeed Yamato's new businesses in 2001. Taisho's portfolio was transferred to this Azami. Then Azami and Yamato (old) merged giving birth Yamato (new) in 2001. Yamato was also an unlisted stock company.

Kofuji (2010b) proposed the observation that this was one example of a stock company having more risk taking tendency than mutual company. At the same time, Kofuji (2010b) pointed out that the president of Yamato (new) did not have insurance but securities business background. As the preceding 7 insurers, the failure of Yamato (new) was ultimately attributable to poor management by the president. Because Yamato (new) was unlisted company too, there appeared to have been no proper governance by shareholders. Therefore you cannot assert that the company was more risk taking thanks to stronger corporate governance, which was the finding by *Keizai Zaisei Hakusho* (Economics Finance Whitepaper by Japanese Government) of 2008. In case of Yamato (new), the president was almighty and not so capable as to avoid bankruptcy. If that is the case, the corporate form whether it is mutual or stock ownership should not be relevant to its corporate governance and solvency.

5. Conclusion

There was assumption, at least theoretically, that mutual ownership was inferior to stock ownership in terms of corporate governance. Although there was not much empirical study in Japan on the issue, majority of the past study was generally affirmative on the predominant existence of mutual companies. Under the circumstances, it was the author's expectation that a case study of the Heisei Life Insurance Crisis might give us some insight on the issue of corporate governance and mutual v. stock ownership, because both mutual and stock companies went bankruptcy. As a result of the study, the followings are the conclusions:

(1) Comparison on mutual versus stock ownership
The presence of stock companies under the 20-company system is very small and mutual and stock companies are far beyond balancing in any way. Therefore it is not very effective to make any comparison using the data or the cases of insurers under the 20-company system. The number of stock companies is only 4 out of 20. Likewise the proportion of total amount of assets is 5.8% for stock companies and 94.2% for mutual companies respectively[5)]. Besides that, if we are to do a comparative study on corporate governance, it is even more important that all stock insurers are unlisted companies. Because they are unlisted companies, you cannot expect that they have such ordinary governance as any normal listed companies would have had. This is especially true for 2 bankrupt companies. Taisho was the smallest in 20 companies. While Kyoei was large enough, they were not only unlisted but rather exceptional in that they were dominated and under the influence by the founder for nearly 60 years. That is to say, the two stock companies are no different than mutual companies in that there was no governance by the shareholders. So, you cannot rebut the assertion that mutual companies or 5 bankrupt mutual companies and stock companies or 2 bankrupt stock companies are not necessarily good examples to make any comparison between mutual versus stock ownership.

(2) "There are mysterious victory and no mysterious loss"
Other than the above (1), 7 insurers are fairly spread and balanced. There were 2 large, 4 medium, and 1 small company, 3 commercial lines and 4 personal lines companies, 4 group affiliated companies, 2 family/founder companies, and 1 independent company (See Table 7). In spite of such diversification, it is rather astonishing to find that most of them have one feature in common. That is the fact there were one dictator in the companies. Those dictators served as the president/chairman or ex-chairman for extraordinarily long time, causing the ultimate reasons for the failure. Nobody could check or control their behavior or they did not have the system to change the dictator or to have capable successor to take over his position. This is the lack of corporate governance. If you have such fundamental and vital shortcomings, it does not matter whether it is mutual or stock ownership. This is analogy of the old war time proverb saying "mysterious victory, no mysterious loss." This means it is easy to find why we lost although it is not so easy to find why we won. In connection with this study, it is easy to identify why they failed and the reason was identical for all the 7 insurers. Therefore, as a case study to make comparison between mutual versus stock ownership, it is more appropriate to take up success cases than failure cases.

(3) The views presented in the existing study
The findings as stated above are generally compatible with the views presented in the existing study (1-(2)). The views which seem to be generally consistent with the findings are as follows:

- While there is some notable tendency that more and more life insurance companies in overseas countries are demutualized recently, I do not see so much significance in demutualization of Japanese companies (Iguchi 2000: 2).
- It is not reasonable that you make comparison between mutual companies and stock companies just from viewpoint of efficiency (Chano 2001).
- It is not very significant to make unilateral comparison between them (Okamura 2006: 226).
- As a result of empirical study in the US, there has been no clear conclusion that either is more efficient than other (Chano 2001).
- There is no evidence that it is a historical certainty that the number of mutual companies will be decreased (Tanaka 2002: 38).
- Whether it is mutual company or stock company is a matter of strategic decision making by management (Yoneyama 2003).

(4) Corporate governance in Japan
There was the hypothesis that as a matter of fact the difference between mutual versus stock ownership does not matter with regards to corporate governance in Japan. That was true after having reviewed the cases of 7 bankrupt insurers. While all 4 stock companies including 2 failed companies were unlisted companies, it must not have made any difference if they were listed companies. In 1990's it emerged as one of the most serious problems that there was no corporate governance in Japan. That was considered to be due to the so called "Japanese style management" where shareholders interest was not so much respected from the viewpoint

of company managers and directors did not do their job of monitoring and checking the execution by managers. As a result, several important revisions were made to the Corporate Law so as to improve corporate governance in 2000s. Therefore it is no wonder that stock insurers were no different than mutual insurers as to the fact that there was almost no governance by the shareholders. As for the insurers who survived the crisis, there is some possibility that there might have been some governance by others than the shareholders and directors or that they happened to have capable managers. There is some evidence that the middle management had such function as corporate governance in large Japanese corporation (Kagono et al. 2010: 257–8). If that was the case with Japanese mutual companies is the subject yet to be substantiated.

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Notes

1) Uemura (2008) put together the reports based on the interviews with 33 people who were involved in the crisis or witnessed as insiders what was going on in those companies before and during the crisis.
2) The issues of mutual versus stock insurers have been extensively studied in the US and there is a large body of literature concerning conflict of interest, expropriation of interest, adverse selection and efficiency issues etc. ranging from Jensen and Meckling (1976), Fama and Jensen (1983) to He and Sommer (2010) etc. Some of the empirical studies are Boose (1990), Cummins and Zi (1998), Jeng and Lai (2005) etc. comparing efficiency between both organizational forms and Mayers and Smith (1986), McNamara and Rhee (1992), Jeng et al. (2007), Erhemjamts and Leverty (2010) etc. examining effects of mutualization and demutualization respectively.
3) The data Yanase et al. (2008) used is the ROA of the 20 life-insurers between1976 and 1995.
4) Oral history means the collection and preservation of any historical information regarding experience by individuals and organizations. It is usually done by interviewing people who participated or witnessed the experience. Oral history strives to gather information from different perspectives and any type of information which cannot be found in written documents. It will serve for many purposes including preservation of history for future generations and is well established and respected discipline in social science. See Mikuriya (2002).
5) The amount of total assets of 4 stock companies was ¥10,575,519 million whereas the amount of total assets of 20 companies was ¥183,585,319 million in 1996.

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