

## Points of Consideration (Examples)

- Disclosure and Transparency
- The Responsibilities of the Board  
(focusing on the fulfillment of their roles/functions, etc. )
- ( ▪ Dialogue with Shareholders )

October 20, 2014

# Disclosure and Transparency

OECD Principles and codes of other countries describe disclosure and transparency. With regard to these matters, are there any points we should keep in mind when we establish the Japanese Code?

OECD Principles, etc.	Points of Consideration (Examples)
<p><u>OECD Principles of Corporate Governance</u>  <i>V. Disclosure and Transparency</i>  <i>The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.</i></p> <p>A. Disclosure should include, but not be limited to, material information on:</p> <ol style="list-style-type: none"> <li>1. The financial and operating results of the company.</li> <li>2. Company objectives.</li> <li>3. Major share ownership and voting rights.</li> </ol>	<p>➤ From the viewpoint of improving the effectiveness of corporate governance, what should we keep in mind in order to ensure that companies make timely and accurate disclosure?</p> <p>→ As for the items currently subject to disclosure (in Corporate Governance Report, etc.), see [Material 3].</p> <p>➤ How should we think about clearly explaining company objectives?</p> <p>→ Already discussed last time</p>

OECD Principles, etc.	Points of Consideration (Examples)
<p>4. Remuneration policy for members of the board and key executives, and information about board members, including their qualifications, the selection process, other company directorships and whether they are regarded as independent by the board.</p> <p>5. Related party transactions.</p> <p>6. Foreseeable risk factors.</p> <p>7. Issues regarding employees and other stakeholders.</p>	<ul style="list-style-type: none"> <li>➤ It is pointed out that the board should establish a policy on determining remunerations for directors and senior managements and disclose such information. What should we think about this point? What about the disclosure of individual remuneration amounts? (Also see pages 7 and 10) [See Material 3]</li> <li>➤ It is pointed out that the board should articulate the basic approach, procedures, etc. of selecting a representative director and other senior managements as well as nominating directors and so on, and disclose such information, and also clearly explain reasons for selecting/appointing each one. What should we think about it? (Also see pages 7 and 10)</li> <li>→ Will discuss the independency of directors at the next Council.</li> <li>→ Already discussed last time</li> <li>→ Already discussed last time</li> </ul>

OECD Principles, etc.	Points of Consideration (Examples)
<p>8. Governance structures and policies, in particular, the content of any corporate governance code or policy and the process by which it is implemented.</p> <p>B. Information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial disclosure.</p> <p>C. An annual audit should be conducted by an independent, competent and qualified, auditor in order to provide an external and objective assurance to the board and shareholders that the financial statements fairly represent the financial position and performance of the company in all material respects.</p>	<p>➤ What should we think about disclosure by companies regarding their basic guidelines/views on corporate governance in response to the Corporate Governance Code? [See Material 3]</p> <p>➤ To ensure that external auditors properly fulfill their roles, what should we think about the following points, for example?</p> <ul style="list-style-type: none"> <li>▪ Establishing standards or policies for proper appointment and evaluation of external auditors</li> <li>▪ Confirming the independency, expertise, etc. of external auditors</li> <li>▪ Securing sufficient time for audit</li> <li>▪ Securing external auditors' access to CEO and CFO (interviews, etc.)</li> <li>▪ Ensuring sufficient coordination between external auditors and corporate auditors/internal audit department</li> </ul>

OECD Principles, etc.	Points of Consideration (Examples)
<p>D. External auditors should be accountable to the shareholders and owe a duty to the company to exercise due professional care in the conduct of the audit.</p> <p>E. Channels for disseminating information should provide for equal, timely and cost- efficient access to relevant information by users.</p> <p>F. The corporate governance framework should be complemented by an effective approach that addresses and promotes the provision of analysis or advice by analysts, brokers, rating agencies and others, that is relevant to decisions by investors, free from material conflicts of interest that might compromise the integrity of their analysis or advice.</p>	<ul style="list-style-type: none"> <li>▪ Companies' responses to the cases where external auditors find any fraud, etc. and ask the company to make appropriate response, or point out any inadequacies or problems</li> <li>➤ What should we think about describing a basic concept that external auditors, who are appointed by shareholders, have responsibilities for the shareholders (although an audit contract itself is concluded with the management) in the Code?</li> <li>➤ What should we think about promoting disclosure in the English language (to the reasonable extent)?</li> </ul>

# The Responsibilities of the Board (focusing on the fulfillment of their roles/functions, etc.)

OECD Principles and the codes of other countries describe the responsibilities of the board.

With regard to the fulfillment of their roles/functions (we will discuss the institutional designs, structures, procedures and other matters concerning the board in the next meeting), are there any points we should keep in mind, when we establish the Japanese Code?

OECD Principles, etc.	Points of Consideration (Examples)
<p data-bbox="188 608 900 651"><u>OECD Principles of Corporate Governance</u></p> <p data-bbox="188 660 815 703"><i>VI. The Responsibilities of the Board</i></p> <p data-bbox="188 713 1057 954"><i>The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.</i></p> <p data-bbox="206 1018 1061 1114">(Annotations to the OECD Principles, VI, 2<sup>nd</sup> and 3<sup>rd</sup> paragraphs)</p> <p data-bbox="210 1123 1084 1415">Together with guiding corporate strategy, the board is chiefly responsible for monitoring managerial performance and achieving an adequate return for shareholders, while preventing conflicts of interest and balancing competing demands on the corporation. In order for boards to effectively fulfil</p>	<p data-bbox="1106 713 2080 906">➤ What roles and responsibilities is the board expected to perform (not limited to making resolutions/approvals on individual matters subject to the resolution/approval of the board)?</p> <ul data-bbox="1160 970 2080 1415" style="list-style-type: none"> <li data-bbox="1160 970 1630 1013">▪ Guiding corporate strategy</li> <li data-bbox="1160 1070 1675 1114">▪ Managing conflict of interests</li> <li data-bbox="1160 1171 2080 1310">▪ Assessing/overseeing the management, taking into account the business performance and potential risks, etc.</li> <li data-bbox="1160 1367 2080 1415">▪ Appointing/dismissing senior managements including</li> </ul>

OECD Principles, etc.	Points of Consideration (Examples)
<p>their responsibilities they must be able to exercise objective and independent judgement. Another important board responsibility is to oversee systems designed to ensure that the corporation obeys applicable laws, including tax, competition, labour, environmental, equal opportunity, health and safety laws. In some countries, companies have found it useful to explicitly articulate the responsibilities that the board assumes and those for which management is accountable.</p> <p>The board is not only accountable to the company and its shareholders but also has a duty to act in their best interests. In addition, boards are expected to take due regard of, and deal fairly with, other stakeholder interests including those of employees, creditors, customers, suppliers and local communities. Observance of environmental and social standards is relevant in this context.</p>	<p>the representative director, and incentivizing them to exercise healthy corporate entrepreneurship (including the avoidance of excessive risks)</p> <ul style="list-style-type: none"> <li>▪ Establishing/reinforcing a compliance structure (instead of checking compliance of each individual business execution) and ensuring a more proactive risk management system is in place</li> <li>▪ Fulfilling their fiduciary responsibility and accountability to the shareholders (includes supporting key executives to make adequate and, timely and decisive decision-making, when the said fiduciary responsibility and accountability are sufficiently fulfilled)</li> <li>▪ Cooperating with diverse stakeholders and considering their opinions</li> </ul> <p style="text-align: right;">etc.</p>

OECD Principles, etc.	Points of Consideration (Examples)
	<p data-bbox="1126 236 2060 331"> <span style="border: 1px solid black; padding: 2px;">Liberal Democratic Party of Japan, Japan Economic Revival Headquarters, “Japan Revival Vision” (abridged)</span> </p> <p data-bbox="1126 339 2000 379">1. (2) Formulation of a Corporate Governance Code</p> <p data-bbox="1151 443 2060 938">           ...We propose that in a similar manner, Japan too should formulate a Corporate Governance Code, which would (a) require strict adherence to comply-or-explain rules, and (b) set forth concrete methods of sound corporate governance for listed Japanese companies, including introduction of independent directors, securing transparency in setting compensation and methods for nominating directors and appointing other top personnel, separation of execution and oversight functions, and practices for top management development and training.         </p> <p data-bbox="1151 954 2060 1345">           ...The effectiveness of corporate governance will be enhanced by (a) clarification of the status of executive officers, and the duties of loyalty that they owe, none of which are prescribed by law; (b) requiring balance among directors from various viewpoints, such as experience, independence, and knowledge; and (c) disclosure of methods of corporate governance and explanation thereof by management. ...         </p>



OECD Principles, etc.	Points of Consideration (Examples)
<p>A. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders.</p>	<ul style="list-style-type: none"> <li>➤ How should we consider the separation of execution and oversight functions?</li> <li>➤ To ensure the board effectively fulfills its oversight function, it is pointed out that balance among directors from various viewpoints such as knowledge, experience and independence is required. What should we think about it?</li> <li>➤ What should we think about the suggestion that clarification of the status of <i>shikkoyakuin</i> and their duties of loyalty are required to be clarified?</li> </ul> <p>*As for the expected roles and responsibilities of <i>kansayaku</i> (and/or <i>kansayaku</i> board), see page 13.</p> <ul style="list-style-type: none"> <li>➤ What should we think about incorporating in the Code directors' fiduciary responsibility, which is expressed as "directors should act in the best interest of the company and the shareholders"? (Also see page 5)</li> </ul> <p>*While the board owes the fiduciary responsibility, what should we think about the importance of their exercising influence over</p>

OECD Principles, etc.	Points of Consideration (Examples)
<p>B. Where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly.</p> <p>C. The board should apply high ethical standards. It should take into account the interests of stakeholders.</p> <p>D. The board should fulfil certain key functions, including:</p> <ol style="list-style-type: none"> <li>1. Reviewing and guiding corporate strategy, major plans of action, risk policy, annual budgets and business plans; setting performance objectives; monitoring implementation and corporate performance; and overseeing major capital expenditures, acquisitions and divestitures.</li> </ol>	<p>the management from an independent/objective standpoint?</p> <p>→ Already discussed last time</p> <p>→ Already discussed last time</p> <p>➤ What should we think about the functions to be performed by the board including, for instance, the following functions?</p> <ul style="list-style-type: none"> <li>▪ Strategic guidance of the company (Also see page 5)</li> </ul>

OECD Principles, etc.	Points of Consideration (Examples)
<p>2. Monitoring the effectiveness of the company's governance practices and making changes as needed.</p> <p>(Annotations)</p> <p>Monitoring of governance by the board also includes continuous review of the internal structure of the company <u>to ensure that there are clear lines of accountability for management</u> throughout the organisation. In addition to requiring the monitoring and disclosure of corporate governance practices on a regular basis, a number of countries have moved to recommend or indeed mandate <u>self-assessment by boards of their performance as well as performance reviews of individual board members</u> and the CEO/Chairman.</p> <p>3. Selecting, compensating, monitoring and, when necessary, replacing key executives and overseeing succession planning.</p>	<ul style="list-style-type: none"> <li>▪ Monitoring the effectiveness of the company's governance practices and making changes as needed <ul style="list-style-type: none"> <li>*What should we think about providing shareholders, etc. with a clear explanation of the scope of execution delegated by the board to the management?</li> <li>*What should we think about self-evaluation (analysis) by the board and self-evaluation by each director?</li> </ul> </li>   <li>▪ Selecting, paying remuneration, overseeing and, when necessary, replacing key executives and overseeing succession planning <ul style="list-style-type: none"> <li>*What should we think about formulation and monitoring of succession plans (plans for successor) for the positions of</li> </ul> </li> </ul>

OECD Principles, etc.	Points of Consideration (Examples)
<p>4. Aligning key executive and board remuneration with the longer term interests of the company and its shareholders.</p> <p>5. Ensuring a formal and transparent board nomination and election process.</p> <p>6. Monitoring and managing potential conflicts of interest of management, board members and shareholders, including misuse of corporate assets and abuse in related party transactions.</p>	<p>Chief Executive Officer (CEO), etc. ?</p> <ul style="list-style-type: none"> <li>▪ Aligning senior management and board remuneration with the longer term interests of the company and its shareholders (Also see page 2)</li> </ul> <p>*It is said that the rate of fixed remunerations for directors and senior managements in Japan is larger than in other countries. What should we think about increasing a performance-linked portion of remunerations, especially the portion linked to medium to long-term performance, etc. as an incentive for sustainable growth?</p> <ul style="list-style-type: none"> <li>▪ Ensuring a formal and transparent board nomination and election process (Also see page 2)</li> </ul> <p>→ Already discussed last time</p>

OECD Principles, etc.	Points of Consideration (Examples)
<p>7. Ensuring the integrity of the corporation's accounting and financial reporting systems, including the independent audit, and that appropriate systems of control are in place, in particular, systems for risk management, financial and operational control, and compliance with the law and relevant standards.</p> <p>8. Overseeing the process of disclosure and communications.</p> <p>E. The board should be able to exercise objective independent judgement on corporate affairs.</p> <p>1. Boards should consider assigning a sufficient number of non-executive board members capable of exercising independent judgement to tasks where there is a potential for conflict of interest. Examples of such key responsibilities are ensuring the integrity of financial and non-financial reporting, the review of related party transactions, nomination of board members and key executives, and board remuneration.</p> <p>2. When committees of the board are established, their mandate, composition and working procedures should</p>	<ul style="list-style-type: none"> <li>▪ Ensuring effective internal control systems, including risk management &amp; compliance systems</li>   <li>▪ Overseeing the process of disclosure and communications (Also see pages 4 and 13)</li> </ul> <p>→ To be discussed next time</p> <p>→ To be discussed next time</p>

OECD Principles, etc.	Points of Consideration (Examples)
<p>be well defined and disclosed by the board.</p> <p>3. Board members should be able to commit themselves effectively to their responsibilities.</p> <p>F. In order to fulfil their responsibilities, board members should have access to accurate, relevant and timely information.</p>	<p>→ To be discussed next time</p> <p>➤ What should we think about directors' access to necessary information and support system (i.e. the use of internal support and advice from outside the company) in order to fulfill their responsibilities appropriately?</p>
<p>● The expected roles and responsibilities of (the board of) <i>kansayaku</i> (Audit &amp; Supervisory Board Member)</p>	<p>➤ What roles and responsibilities are expected to be fulfilled by <i>kansayaku</i> (and/or <i>kansayaku</i> board)?</p> <ul style="list-style-type: none"> <li>▪ Auditing business execution by directors</li> <li>▪ Contributing to discussions at the board</li> <li>▪ Determining proposals to the general shareholders' meeting concerning selection/dismissal of external auditors, exercising their consent rights to remunerations for external auditors, etc.</li> </ul> <p>➤ To what extent, should <i>kansayaku</i> (and/or <i>kansayaku</i></p>

OECD Principles, etc.	Points of Consideration (Examples)
	<p>board) be able to be involved in questions of ‘appropriateness of judgments made by management’ beyond questions of compliance?</p> <ul style="list-style-type: none"> <li>➤ To what extent, can <i>kansayaku</i> (and/or <i>kansayaku</i> board), who do not have voting rights in the board, be able to influence decision-making of the board?</li> <li>➤ What should we think about professional knowledge and experience required of <i>kansayaku</i>?</li> <li>➤ It is pointed out that <i>kansayaku</i> (and/or <i>kansayaku</i> board) should include person(s) with knowledge of finance/accounting. What should we think about it?</li> <li>➤ What should we think about the structure necessary for <i>kansayaku</i> (and/or <i>kansayaku</i> board) to effectively fulfill their responsibilities? (securing personnel/budgets for supporting <i>kansayaku</i>; cooperation and information sharing with the management, internal audit department, outside directors, external auditors, etc. )</li> </ul>

# ( Dialogue with Shareholders )

Some members suggest at the last meeting that the Code should include actions to be taken by the companies to facilitate constructive dialogue between companies and their shareholders, taking the Japan's Stewardship Code into account. In response, it will be an option to describe 'dialogue with shareholders' as an independent topic. Based on the above, what should be kept in mind, when we establish the Code in Japan?

## Corporate Governance Codes in Other Countries etc.

### The UK Corporate Governance Code

#### E.1: Dialogue with Shareholders

##### Main Principle

There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.

##### Supporting Principles

Whilst recognising that most shareholder contact is with the chief executive and finance director, the chairman should ensure that all directors are made

## Points of Consideration (Examples)

- Through the formulation of the Japan's Stewardship Code, institutional investors are now required to have constructive engagement (purposeful dialogue) based on in-depth knowledge of the investee companies and their business environment. What should investee companies consider the meaning of such 'dialogue' to be?



## Corporate Governance Codes in Other Countries etc.

aware of their major shareholders' issues and concerns.

The board should keep in touch with shareholder opinion in whatever ways are most practical and efficient.

### Code Provisions

E.1.1. The chairman should ensure that the views of shareholders are communicated to the board as a whole. The chairman should discuss governance and strategy with major shareholders. Non-executive directors should be offered the opportunity to attend scheduled meetings with major shareholders and should expect to attend meetings if requested by major shareholders. The senior independent director should attend sufficient meetings with a range of major shareholders to listen to their views in order to help develop a balanced understanding of the issues and concerns of major shareholders.

## Points of Consideration (Examples)

- What should be taken into consideration by investee companies to realize 'constructive dialogue'? For instance, what should we think about the following points?
  - Establishing/improving the structure through the clarification of persons (institutions) who manage overall dialogue with shareholders and pay careful attention to realize constructive dialogue
  - Persons in charge of actual dialogue (face-to-face contacts) with shareholders
  - Ensuring internal collaboration with IR, Corporate Planning, Finance, General

## Corporate Governance Codes in Other Countries etc.

E.1.2 The board should state in the annual report the steps they have taken to ensure that the members of the board, and in particular the non-executive directors, develop an understanding of the views of major shareholders about the company, for example through direct face-to-face contact, analysts' or brokers' briefings and surveys of shareholder opinion.

### A.3. The Chairman

#### Supporting Principles

...The chairman should ensure effective communication with shareholders.

France "Corporate governance code of listed corporations"

## 2. The Board of Directors and The Market

### 2.1 Corporations' communications to the market

2.1.4 The Board should ensure that the investors receive relevant information, which is

## Points of Consideration (Examples)

Administration, Legal and other departments

- Providing feedback to senior management and the board concerning shareholders' opinions acquired through dialogue, etc.
- Methods for dialogue other than individual meetings (e.g. investor briefings and IR activities)
- Disclosure of the above-mentioned policies and initiatives

And other topics

- Some argue that companies should make efforts to identify their major shareholders (actual owners of shares), and shareholders are also expected to cooperate with such companies' investigation to the greatest possible extent. What should we think about it?

## Corporate Governance Codes in Other Countries etc.

balanced and enlightens them about the strategy, development model and long-term strategies of the corporation.

### Singapore “Code of Corporate Governance”

15 Companies should actively engage their shareholders and put in place an investor relations policy to promote regular, effective and fair communication with shareholders.

15.1 Companies should devise an effective investor relations policy to regularly convey pertinent information to shareholders. In disclosing information, companies should be as descriptive, detailed and forthcoming as possible, and avoid boilerplate disclosures.

15.3 The Board should establish and maintain regular dialogue with shareholders, to gather views or inputs, and address shareholders' concerns.

## Points of Consideration (Examples)

## Corporate Governance Codes in Other Countries etc.

### ICGN Global Governance Principles

#### 1.3 Dialogue

The board should make available communication channels for periodic dialogue on governance matters with shareholders and stakeholders as appropriate. Boards should clearly explain such procedures to shareholders including guidance relating to compliance with disclosure and other relevant market rules.

### "Japan Revitalization Strategy" Revised in 2014

#### Section 2 I 1 (3) i)

In order to increase corporate profits through improvement of productivity and ensure that the increased profits lead to increase of wages, reinvestment and the return of profits to shareholders, it is important – primarily for global companies – to achieve sustainable increases in corporate value by giving consideration to the cost of capital and enhancing corporate governance. ...

## Points of Consideration (Examples)

- It is pointed out that in order to achieve sustainable growth, companies are required to establish business strategies and business plans, articulate medium to long-term earnings plans and capital policy, and set the target for profitability and capital efficiency, and then clearly explain those matters to shareholders, etc. with words and logic comprehensible to them. What should we think about this point?