

**Minutes of the 8<sup>th</sup> Council of Experts**  
**Concerning the Corporate Governance Code**

1. Time and date: 4:30–6:00 pm, December 12 (Friday), 2014
2. Place: Financial Services Agency

[Ikeo, Chairman] It's already the scheduled opening time, and all the prospective attendees are here. So I'd like to open the eighth Council of Experts Concerning the Corporate Governance Code. Thank you very much for taking time from your busy schedule for the Council.

I would like to start the proceedings. Today we will hold a discussion, keeping in mind that the proposal of the Code must be completed. I'd appreciate in advance for your cooperation.

For that purpose, today the secretariat prepared Materials 1 and 2. These are the drafts which are partly modified based on your opinions in the last meeting, and newly added the Preamble. Material 1 shows additions and changes by using Track Changes, and Material 2 is the final version after accepting all changes.

After the last meeting, several members submitted comments on modification of the working draft of the Code. The secretariat prepared Material 1, taking those comments into account. You can find those comments from the members on the table, so I will not read them out here. My paper does not really contain a comment or opinion. I just thought it would be better explained in writing rather than orally.

First, the secretariat will be explaining the draft of the Code, and then we will be discussing it. Now I'm handing it over to the secretariat for the explanation.

[Yufu, Director of the Corporate Accounting and Disclosure Division] I'll explain the draft. Please look at Material 1. If you flip a page, you'll find newly added Preamble. I'm sorry if you have trouble reading the red font. I'll explain it in sequence.

At the beginning of the Preamble, we put a box to explain the definition of corporate governance in this Code and this Code based on the Cabinet approval.

Under the box, the Background is presented. Item 1 states that initiatives for corporate governance system have significantly accelerated in recent years. Following that, as specific examples, Item 2 refers to the formulation of Japan's Stewardship Code and the revision of the Companies Act; and Item 3 refers to the establishment of JPX-Nikkei Index 400.

Item 4 is about the background of this Council of Experts, stating that it was established in response to the Japan Revitalization Strategy which was revised this year, and has engaged in discussions. It also states that the content of this Code is based on the OECD Principles. Item 5 states that the Code and its English translation are to be published domestically and globally for public comments. Then, TSE is expected to amend the listing rules and other relevant regulations and establish the Corporate Governance Code which has the same content of the draft.

Objectives of the Code are described in Item 6 and thereafter. The content of Item 6 is very similar to what is written in the box at the beginning.

Item 7 begins with a sentence, which reads “(i)t is important that companies operate themselves with the full recognition of responsibilities to a range of stakeholders, starting with fiduciary responsibility to shareholders who have entrusted the management.” As the term “fiduciary responsibility” is repeatedly used thereafter, we explained the term in this paragraph.

After such an explanation, the next sentence continues that the Code seeks “growth-oriented governance” by promoting timely and decisive decision-making based upon transparent and fair decision-making through the fulfillment of companies’ accountability in relation to responsibilities to shareholders and stakeholders. Then it continues that this Code does not place excessive emphasis on avoiding risks or preventing corporate scandals, but principally aims at stimulating healthy corporate entrepreneurship, and supporting sustainable corporate growth and increase corporate value over the mid- to long-term.

In the next paragraph, it reads that the Code includes language which calls for a certain measure of corporate self-discipline. It continues to read that it is, however, not appropriate to view such descriptions as limits on business activities of companies. Indeed, quite the opposite: without appropriately functioning corporate governance, the reasonableness of management’s decision-making processes cannot be secured. In such a case, the management may become risk-avoiding due to concerns that their responsibility with respect to business decisions may be put in question. Such a situation would significantly restrict decisive decision-making and companies’ business activities. By calling for appropriate corporate governance disciplines at Japanese companies, the Code aims to have the management free from such restrictions and establish an environment where healthy entrepreneurship can flourish and where the management’s capabilities can be given full force.

We consider that Item 8 also includes an important message. It writes about the relationship with short-termism in the market place. It is expected that the Code encourages mid- to long-term investments. Market participants who have the strongest expectations for improvements of corporate governance are usually shareholders with mid- to long-term holdings, and they usually wait until such improvements are achieved. Following that, the Code describes that such shareholders have the potential to become important partners for companies.

Then, I skip one sentence following that. It describes about corporate initiatives to be taken in accordance with the Code. Such initiatives can be further enhanced through constructive “purposeful dialogue” between shareholders (institutional investors) and companies under the Stewardship Code. In that sense, this Code and the Stewardship Code are “the two wheels of a cart”, and it is hoped that they will work appropriately and together so as to achieve effective corporate governance in Japan.

The next section is concerning the “Principles-Based Approach” and the “Comply-or-Explain Approach”. Item 9 explains that the Code specifies General Principles, Principles and Supplementary Principles; and how to implement those principles may vary depending on characteristics of individual companies. It is described that the Code’s principles should be applied in accordance with each company’s particular situation.

Item 10 explains the rule-based approach vs. principles-based approach. Please look at the second paragraph of Item 10. Under the principles-based approach, it is important for individual listed companies to judge whether or not their activities are appropriate in light of the aim and spirit of the principles, not by checking against the literal wording of the principles. For this reason, the terminology used in the Code is not strictly defined as is the case with laws and regulations. It is anticipated the companies that are accountable to shareholders and other stakeholders will apply appropriate interpretations of the terminology in accordance with the aim and spirit of the Code. Shareholders and other stakeholders are also expected to fully understand the significance of this principles-based approach.

Item 11 provides an explanation of the comply or explain approach. From the fourth line of Item 11, it explains that if a company finds specific principles inappropriate to comply with in view of their individual circumstances, they need not be complied with, provided that the company explains fully the reasons why it does not comply.

As for Item 12, please take a look at the second line. It states as follows: It is necessary to bear fully in mind that companies subject to the Code are not required to comply with all of its principles uniformly. In this regard, not only the companies, but also shareholders and other stakeholders are expected to fully understand such an intention, and respect particular circumstances of individual companies. In particular, it is not appropriate to consider the literal wording of each principle of the Code superficially, and conclude automatically that effective corporate governance is not realized by a company on the ground that the company does not comply with some of the principles.

The sentence starting from “(o)f course” describes that when companies explain their reasons for non-compliance, they should ensure shareholders and other stakeholders fully understand such an explanation. Offering a superficial explanation using boiler-plate expressions would be inconsistent with the concept of “comply or explain”.

Item 13 is about companies subject to the Code. In the first line, it states that it is applicable to all companies listed on securities exchanges in Japan. In this regard, during the previous meetings of this Council, some members suggested that it should be applied only to companies listed on the TSE First Section, or a certain group within the TSE First Section. While the First Section and Second Section are collectively called as the Main Markets, from the viewpoint of the market system, the system designs of First and Second Sections are quite similar except for the liquidity of stocks. Therefore, it is written that the Code is applicable to companies listed on First and Second Sections.

What is mentioned next – from the second line – is that when this Code is applied to companies listed on markets other than Main Markets, certain considerations may be required to be given to the size and characteristics of such companies, for instance, in terms of governance structures and disclosure. The last sentence states that the TSE is expected to figure out what considerations are required for which parts of the Code.

Item 14 refers to three institutional designs under the Companies Act, and specifies that the Code does not recommend any particular form of design among these three. As for principles referring to *kansayaku* and Companies with the *Kansayaku* Board, companies which adopted other forms of institutional design are expected to apply the principles by making necessary adjustments in accordance with their forms.

Item 15 refers to the timing of implementation. It is expected that the Code will enter into force on June 1, 2015, after the TSE takes necessary institutional steps. While Council has discussed this point in previous meetings, as we understand that the Cabinet decision was made on the assumption that it would be implemented in June [2015], in other words, to be in time for the next general shareholder meeting season, we described Item 15 in this way.

However, there is an additional explanation in the second paragraph. There may be companies that will find it difficult to fully implement certain principles from the implementation date, even if they desire to do so, such as the principles on governance structures. In such situations, if companies undertake serious investigations and preparations for the commencement of the Code's application but still find immediate full compliance difficult, providing clear explanations on their plans and conceivable schedule for future compliance should not be ruled out as being against the Code.

Moreover, the third paragraph reads that the Code contains some principles which require disclosure or explanation, including cases where companies are asked to "explain" the reasons for non-compliance. Since it would be desirable that companies disclose and explain some of these matters in a standardized framework, the TSE is expected to offer clarification for handling this matter.

Item 16 specifies that the Code does not remain unchanged, and it concludes by saying that it is anticipated that the Code will be periodically reviewed for possible revisions.

Now I'll be explaining some revisions made since the last meeting on November 25. Please turn to page 12. I will not explain minor revisions just to unify spelling or wording variations as shown in 1.2.2. A phrase is added to 1.2.3 in response to the member's comment at the last meeting.

Please turn to page 14. At the last meeting, we received a suggestion on Principle 1.3 from the members. Previously, we used such an expression as "basic strategy for mid- to long-term capital policy". Now we deleted the term "mid- to long-term" which specifies time horizon. Depending on circumstances of individual companies, there would be cases where companies cannot present their mid- to long-term policies, or, on the contrary, companies should rather present short-term policies. We, therefore, excluded the specification of time horizon. Due to the similar reason, we deleted the term "mid- to long-term" from several subsequent principles. Furthermore, since readers may associate the expression "basic strategy for capital policy" with a highly specific strategy, we changed the expression to "explain their basic strategy with respect to their capital policy".

Let me skip up to page 20. Please look at Principle 3.1(v) in the box on page 20. This was also discussed during the last meeting. Basically, we still consider it important that companies providing explanations regarding nominations of individual candidates for directors and *kansayaku* in accordance with (iv), and thus changed the expression to "explanations with respect to the individual appointments and nominations based on (iv)".

Please turn to page 22. We received an opinion paper from a member, which is distributed to you. We changed the order of a few sentences.

Please turn to page 23. As for Supplementary Principle 4.1.1, the description of the previous draft was insufficient, as a member pointed out in his opinion paper. The intention of 4.1.1 is that the board is expected to disclose which matters are to be decided by the board

and which matters are to be delegated to the management. Generally, each company has a very thick file for matters to be discussed by/reported to the board. Our assumption was not the disclosure of such a file itself, but the overview. Accordingly, it was modified to that effect.

Another revision was made to 4.1.3. This was discussed during the last meeting, and we also received an opinion paper referring to this point. Previously, we wrote “approve a succession plan”, but it may give readers the impression that a “succession plan” or other similar documents must be submitted to the board for resolution. However, we consider it essential that the board adequately oversee planning for successors rather than the preparation of such documents, and thus rephrased as “engage in the appropriate oversight of succession planning”.

I’m moving on to Principle 4.3 on page 24. The previous description was insufficient. As for the target to be assessed [with respect to appointment/dismissal], as shown in 4.3.1, it should be “senior management”. We originally assumed key members of the management, so we modified it to read as “senior management”.

Please take a look at 4.4.1 on page 26. We made a similar revision to 4.8.2 as well. In response to an opinion paper, we modified the expression to “*kansayaku* or the *kansayaku* board”.

Principle 4.5 used to read “(b)earing in mind their respective fiduciary responsibilities ... the directors, *kansayaku* and the management ...” However, in the earlier part of the Code, it is described that the management may include officers called *shikkoyakuin*, whose position is not a statutory one. These *shikkoyakuin* include employees and accordingly, we modified the expression in a way to avoid the conclusion that they too have “their respective fiduciary responsibilities”.

We also revised Principle 4.7 (i), taking into account the members’ opinions during the last meeting.

As for the following 4.7 (ii), the previous statement could be interpreted as “evaluation and appointment/dismissal [of senior management] and other important decision-making”. Certainly “appointment and dismissal” are “decision-making” to be resolved by the board, yet “evaluation” isn’t. Besides, Principle 4.3 on the previous page describes evaluations in detail, so we consider it is not necessary to refer to it in this principle again, and thus omitted the term “evaluation”.

On page 27, we added a paragraph to the [*Background*], in response to the members’ opinions at the previous meeting.

As for Principle 4.9, some descriptions, which were previously pending, are now added. The first sentence states that the board should establish and disclose independence standards aimed at securing effective independence of independent directors, taking into consideration the independence criteria set by securities exchanges.

In the [*Background*], it is explained that the independence criteria and related disclosure requirements established by securities exchanges leave a considerable room for interpretation. While they are appreciated for ensuring flexibility, it is also pointed out that varying interpretation by institutional investors and proxy advisors results in an adverse effect of making companies apply these criteria too conservatively. Moreover, Japan’s

exchange criteria differ from those of other countries in several regards. Then it concludes that the Council of Experts expects that, while taking into account future developments, securities exchanges will undertake appropriate reviews as necessary.

On page 29, an additional example is introduced in relation to Company with Audit and Supervisory Committee, a new form of company [under the amended Companies Act], based on the proper understanding of this institutional design.

Now I'm moving on to page 31 – Supplementary Principle 4.13.1. We received an opinion paper concerning this part. To describe “including” in the phrases “directors including outside directors” and “*kansayaku* including outside *kanasayaku*” in the Japanese language, we avoided the use of the expression “*hajime*” which can be deemed to prioritize, and now use such a neutral expression as “*fukumu*”. [*Translator's note: This discussion is applicable only to the Japanese version. The English version remains unchanged.*]

On page 33, we added the term “engagement” so that it reads “purposeful dialogue (engagement)”, aligned to the Stewardship Code.

As for Principle 5.1 on page, in response to the discussion at the last meeting as well as members' opinions, we edited the caption and content. Revisions to Principle 5.2 were made for the same reason I explained earlier.

That's all for my explanation.

[Ikeo, chair] Thank you very much. Taking the secretariat's explanations into account, please express your opinions or ask questions concerning Materials 1 and 2.

Mr. Horie, please go ahead.

[Horie, member] Thank you. The Preamble clarifies that the Corporate Governance Code provides the framework for enabling transparent, fair, timely and decisive decision-making. The objectives of the Council are clearly articulated, and I really think it is excellent. What is written in the Preamble is really great. I'd like to thank the secretariat for tremendous efforts.

Based on this Code, I'd like to make several requests to the management, from the standpoint of an institutional investor. Considering the aim of this Code, I'd like the management to draft the corporate policy to address the Code. This is my biggest request. Japanese people tend to comply with everything. I hesitate to say this in front of legal experts, but I'm concerned about a potential risk of drafting the Code from the legal perspective, which I think is wrong.

I would point out the possibility that the same thing is happening under the Stewardship Code. I'd like them to establish policies to address the Code, based on their ability to identify medium to long-term corporate value. However, there would be some fund managers which just comply with all principles before they acquire such an ability. Such an attitude is obvious to professionals. Even though they comply with all principles, professionals can see at a glance that there is no substance. Accordingly, I'd like business companies to avoid drafting policies just for formality. The Preamble made this point very clear as the intent of Comply-or-Explain approach. Investors who seriously look at medium to long-term corporate value will never rate “Explain” lower than “Comply”.

There are various business environments. For instance, in case a company is undergoing restructuring and the management must make managerial decisions very quickly, if the managing board led by CEO who has plenary authority quickly makes decisions and takes

actions, there will be no problem from the viewpoint of investors. In other words, investors highly appreciate explanations in accordance with particular circumstances of individual companies. I really believe that companies should not draft [their policies concerning corporate governance] with boilerplate stipulations requiring compliance without any exception. I'd like to request that the policies are written by top management, if possible, or those who actually engage in management such as corporate planning, in a manner to ensure the effectiveness, from the viewpoint of management.

I think such policies will play an important role as counterparts to CEO shareholder letters seen in other countries. As you know, in other countries, if you read CEO letters written by Jamie Dimon of JP Morgan or Warren Buffett of Berkshire Hathaway, you can find basic matters enabling you to judge future corporate value. I hope companies positively consider that the Corporate Governance Code provides a good opportunity to clearly articulate to investors about their corporate management in pairs with CEO letters, and such matters are written by taking corporate value into account from the corporate management perspectives. This is a request from the viewpoint of an investor.

[Ikeo, chair] Thank you very much. Mr. Toyama, please go ahead.

[Toyama, member] In response to Mr. Horie's comment, I'd like to make comments from a management's standpoint.

First of all, I would like to pay my respect to the secretariat – the Financial Services Agency and the TSE – for preparing such a great draft in an extremely limited time. And I would also like to express my gratitude to Chairman Ikeo and all the members for very constructive discussions, probably despite assumingly different standpoints and past background – it may sound like self-praise as I'm also a member, though.

I also consider the content of the Code is probably just right at the moment, without any excess or deficiency, like a perfect landing of gymnast Kohei Uchimura. I have no request for modifications. I don't think there is any point to be modified.

In response to Mr. Horie's comment, as mentioned at the beginning, since Abe's second Cabinet was established, various initiatives have taken place: the Stewardship Code under the Financial Services Agency; the revision of the Companies Act under the Ministry of Justice; the Government Reform Investment Fund (GPIF) Reform under the Ministry of Health, Labour and Welfare; the launch of JPX400 at TSE; the issuance of the Ito Review concerning the engagement or constructive dialogue between companies and investors under the Ministry of Economy, Trade and Industry; and this Corporate Governance Code. Each of these are reform-oriented, and now they are all converging.

In addition, the so-called *gojuuku*, *rokujuuku* problem is being resolved under Abenomics. So it could be said that the stage is set toward sustainable revitalization – enhancement of earnings power. Therefore, in my opinion, companies and investors don't have any excuses anymore. Whether or not sustainable growth and increased corporate value can be achieved by making the best use of such environment is up to businesses and industries, as just mentioned.

I think I have told this at first or second meeting of this Council of Experts. As things turned out, in the past 20 years, Japan's listed companies have seen a decline in their share of sales in the world market, a decline in profitability in terms of ROE which used to be higher

than that of the US companies in the past, a decline in market capitalization, and even a decline in their share of employment within Japan. These declines are statistical facts.

Have all these resulted from losing in the competition with emerging countries? As I recall, the percentage of Japanese companies in Fortune 500 decreased to one-third of the peak level, while the percentages of US and European companies decreased probably only by 10 to 20 percent. Therefore, Japanese companies have been losing in relative terms. Furthermore, the ROE of Japanese companies used to be higher than that of the US companies. As clearly shown in the Ito Review, the slump of ROE is due to a decline in ROS, not the leverage. In short, Japanese companies have been losing competitiveness. This is also obvious.

In addition, employment has suffered on a long-term basis. Then I don't think it is reasonable to lay the blame of this super-long term stagnation for almost a quarter century to the *gojuuku* issue. Japan has such a high level of technical strength and *gemba* power (on-site capabilities), which win international recognition. As the Ito Review also mentioned, the fact Japan lost so many things despite the high recognition is attributable to the top management structure of companies. Indeed, as the saying goes, "who spits against Heaven, spits in his own face". I think we should honestly admit that the responsibility lies with us, and reflect on where we went wrong.

The social significance of companies is primarily to grow sales, increase revenues, increase quality employment opportunities and labor income, pay taxes, push up their stock prices, and increase asset income at household level through an investment chain. When viewed in hindsight, it is true that we could not fully achieve them, although there were various unfavorable conditions.

Meanwhile, after World War II, our older generations achieved Japan's industrial recovery from a much severer situation than the *gojuuku*, *rokujuuku*. What our older generations did at that time was probably to understand essential advantages of Japanese companies in one hand, and actively adopt excellent management models and management techniques of Western countries on the other hand. And with Japanese spirit combined with Western leaning, they assimilated such models and techniques in a way to fit well in Japan, and established new models, which later gained international reputations as Japanese-style management or Japanese-style quality control.

However, since Japanese-style management was praised by saying "Japan as Number One", I think we have become conceited, arrogant. I'm afraid many top management of Japanese companies have weakened their abilities to pursue self-reform without sanctuary, maintain painful self-reform, or evolve. Arrogance extinguishes diligence. Without diligence, people tend to have a victim mentality toward the pressure to change. I have an impression that discussions concerning corporate governance have been swinging between arrogance and the victim mentality. I've been participating in various discussions in the past 10 years, and I honestly feel like that.

But, fortunately, many people in businesses and industries are now willing to reinvent Japanese-style management, while Japanese companies once again have Japanese spirit combined with Western leaning, and accelerate the evolution without sanctuary. Certainly, this is the determination shared by many people. At the same time, they share a perception



that companies can afford no further delay.

I have almost no doubt that the Code will encourage some management who are willing to undertake reform. From my own experience, I don't think that a series of governance reforms, including this Code, contradict core competence of "the community" in Japan. Furthermore, they cannot be called core competence or culture if they are undermined by the reform. If some people claim this, I think they are trying to replace their problems with something else.

In other words, the stage was set in 2014. After 20 or 30 years, will our younger generations look back the year 2014 as the first year of new corporate governance, or the year when Japanese companies started to revitalize their earning power? As Mr. Horie mentioned, I think the answer would be up to the enthusiasm and diligent efforts of us, the current management.

For instance, concerning the media report of the number of outside directors, we should think about it rationally. There are around 3,000 listed companies in Japan. Suppose the term of office for CEO is 6 years. Then we have 500 new ex-CEOs every year. In the past 10 years alone, we have 5,000 ex-CEOs. If these people concurrently serve as director of two companies, we can secure a total of 10,000 outside directors. Japan has access to such a talent pool. Considering that Japanese people live long, many of them must still be in good health. If they are deemed not qualified for the job, it raises the question about whether these people were actually acting as CEOs of listed companies. The claim that it is difficult to find candidates would therefore be "who spits against Heaven, spits in his own face".

I'll finish my this in a minute. Anyway, with the Corporate Governance Code as the driving force, I expect, and am confident that diligent efforts and strict self-reform concerning how corporate management should be will be made, and the next two decades will be decades of winning back revenue share in the world market, profit level, and quality and quantity of employment, which Japanese companies lost in the past two decades. That's all.

[Ikeo, chair] Thank you very much.

Mr. Oguchi, please go ahead.

[Oguchi, member] Thank you. First, I'd like to share my impression of the draft, and then ask a question for confirmation. This Council was established in response to the Japan Revitalization Strategy (Revised in 2014). As I mentioned in the second Council, our mission is to ensure that "the Code will, while reflecting the circumstances of Japanese companies, aim to attain international reputation" – sort of antinomy. We have continued discussions, while facing such a challenge and being exposed to a risk of falling between two stools.

Some members place emphasis on international reputation, and other members put weight on the circumstances of the companies. Nonetheless, we listened to each other's opinions and had constructive discussions. Partly owing to that, and partly owing to the efforts of the secretariat, such a convincing draft was prepared in such a short time. I really appreciate it and am also proud of it.

As I mentioned at the first Council, discussions on the Corporate Governance Code necessarily tend to center round the roles and functions of the board. Certainly, these points

are essential, and thus inevitably draw public attention. Yet if I recall, I rather consider that other principles, which are included in the draft as a result of our discussions, will become agenda for facilitating constructive dialogue between listed companies and shareholders.

I cannot refer to everything due to the time constraint, but as Supplementary Principle 1.1.1, the following text has been added: When the board recognizes that a considerable number of votes have been cast against a proposal by the company and the proposal was approved [at the general shareholder meeting], it should analyze the reasons behind opposing votes and why many shareholders opposed, and should consider the need for shareholder dialogue and other measures. This principle corresponds to an additional to the UK Governance Code revised in September, which I think is the most progressive code, about which we also referred to at this Council. That expression is included in the draft proposal we prepared for the first time.

As this example shows, the draft includes a lot of progressive contents. Listed companies are going to engage in dialogue with shareholders based on those contents. Taking Supplementary Principle 1.1.1, if companies view the exercise of voting rights as an opportunity to reflect shareholders' voices for the business management, instead of being remained caught up in black-or-white thinking – feeling happy about an approval or disappointed about an denial – and have dialogue with shareholders, and if actually contributes to increasing corporate value, this principle will win high recognition. The Ito Review displayed a message that Japan aims at becoming an advanced country in the area of dialogue or engagement, and I think this principle will go along with that.

Mr. Horie earlier referred to the Stewardship Code. I also participated in the Council for the Stewardship Code. Speaking from the experience with that code, at first, the disclosure of voting results drew focused attention, because it is an easy-to-understand point of discussion, and it cannot be helped. As the content of the Stewardship Code were being widely known, people started substantive discussions, such as “what is constructive and purposeful dialogue to facilitate the sustainable growth of investee companies?”

Similarly, in case of the Corporate Governance Code, it would be inevitable that public attention goes to easy-to-understand issues such as the number of independent directors. Nonetheless, I think the Corporate Governance Code will take the same path as the Stewardship Code: in other words, points of discussion will shift from the formality to substance. From now on, I assume that a lot of discussions or dialogues on this Code will take place within and outside of Japan. As the members of this Council, including myself, obtained various insights here, I think we are responsible for actively participate in such discussions, and effectively increase the significance of this Code, which we have worked out. I'm sorry for taking a long time. That's all for my impression.

As for my question, I'm afraid it may be too specific. In Item 13 of the newly added Preamble, it reads that the Code is applicable to companies listed on securities exchanges. And Principle 1.4 on page 14 refers to cross-shareholdings. With regard to cross-shareholdings, let me refer to the current situation of cross-shareholdings by banks as an example. Strictly speaking, the reality of cross-shareholdings is that shares in question are not held by holding companies of listed companies, but unlisted subsidiary banks. It would not be limited to banks. While the Code is applicable to listed companies, such shares may

be held by their unlisted subsidiaries. In such cases, what do you think about the application of the Code?

[Ikeo, chair] May I hand it over to the secretariat?

[Yufu] As Mr. Oguchi has pointed out, for cross-shareholdings by banks, we are aware that such shares are held by not only listed holding companies, but also unlisted subsidiary banks. In this regard, as the Code takes the principles-based approach, I think it is anticipated to take necessary actions considering the aim and spirit of the Code. I believe that applicable companies will naturally take necessary actions including shares held by their unlisted subsidiary banks.

[Ikeo, chair] There are many group companies. In their cases, I think they would make considerations including the governance structure of the entire group.

Are there any other opinions? Mr. Mori, please go ahead.

[Mori, member] Thank you. While there were diverse opinions, the secretariat drafted the Code by incorporating such opinions in a short period. I'd like to express my respect for the efforts of the secretariat. Furthermore, because drafting the Corporate Governance Code is required as one of the first emergency measures under the Government's growth strategy, despite various views, I think corporate governance must be fully addressed from now on.

I believe that the Code will contribute to improving corporate governance in Japan, and help domestic and foreign stakeholders understand corporate governance in Japan. I do think drafting this Code was very much meaningful.

Let me make several comments. I have been talking about the importance of disclosure. In order to obtain profound understanding of domestic and foreign stakeholders, I believe how to disclose information is critical. Thus I mentioned that we should fully consider such matters as the scope, content, reliability and timeliness of disclosure, and incorporate them into the Code.

The Code does not supersede laws and regulations. It may be further discussed in the future; but for instance, Supplementary Principle 1.2.2 stipulates that while ensuring the accuracy of content, listed companies should strive to send convocation notices for general shareholder meetings early enough to give shareholders sufficient time to consider the agenda. Exactly. In order for shareholders to exercise their rights at the general shareholder meetings, they need time to sufficiently analyze information. On the other hand, unless the reliability of the information is ensured, it will just cause confusion. Therefore, I'd like to place emphasis on "while ensuring the accuracy of content".

Furthermore, at this Council, I stressed the importance of accountability. General Principle 4 emphasizes the importance of accountability along with fiduciary responsibility. I think it is very meaningful for this Code. Accountability is closely related to the reliability of information. I think it important to explain reliable information in a timely manner.

It is very significant for this Code that the board and other responsible parties recognize their accountabilities once again. Concerning Principle 4.11, I expressed my opinions about expertise in auditing in relation to the reliability of information. The Code refers only to expertise in finance and accounting. I understand that my opinion was not reflected to this principle, because the codes of other countries, in general, do not refer to auditing.

In other countries, the term "experts" is used to refer to those who have expertise in

finance and accounting. Actually, it is often the case that when some people are called experts in finance and accounting they include persons who have experience in auditing. I think such a situation is different from Japan's corporate governance environment. I'd like to emphasize that in my understanding, expertise in finance and accounting includes expertise in auditing, considering the reality of other countries.

I wanted to stress these 3 points. Thank you very much.

[Ikeo, chair] Thank you very much.

Well, Ms. Nakamura, please go ahead.

[Nakamura, member] Similarly to other members, I first would like to thank the secretariat for compiling opinions of all the members in such a short time.

I'd like to express opinions from the standpoint of corporations. I think this Corporate Governance Code will become like a communication tool between companies and investors. In the days to come, each company reads the Code carefully, and expresses how they consider each matter in their own words; investors express opinions about it; through such interactions, corporate governance of each company improves. I think such a process is essential.

Based on such an assumption, I'd like to make some requests. Item 15 on page 6 states that the Code will enter into force on June 1, 2015. Furthermore, I assume some will take form of the revision of the Corporate Governance Reports.

Companies need to consider how they express their response to the Code. As I mentioned earlier, companies need to carefully examine each principle, and identify which ones have already been complied with, and which ones are not. As for the former ones, they need to express the current status. As for the latter ones, they need to plan and consider how to address them. So I assume that practically there should be a significant amount of tasks. Other companies also state that it is very hard to implement effective from June 1, 2015.

Therefore, as of June 1, 2015, I assume companies will still be in a preparation stage concerning some parts of the Code. I'd like shareholders and investors to understand such a situation. That's my request.

That's all.

[Ikeo, chair] Thank you very much.

I'd like to hear more opinions or comments. Mr. Uchida, please go ahead.

[Uchida, member] First of all, I'd like to express my respect for preparing this draft within a short period despite a wide range of opinions. I think it was tough.

I do not have any comment on the Preamble, which was presented today. Concerning other matters, I already submitted my opinion paper, so I won't refer to them here.

I have three requests concerning the administrative aspect. First, the Preamble offers concise explanations of the principles-based approach and comply-or-explain approach in an easy-to-understand manner. As I mentioned in the last meeting, companies are not familiar with these approaches. Besides, time is limited before the next general shareholder meetings. To enable companies take necessary actions upon fully understanding the intention of the Code, I'd like to request you to ensure that the Code is widely known through explanatory meetings and other ways, not just publishing the Code. I believe Keidanren (Japan Business Federation) will cooperate.

Furthermore, I'd like to request you to fully alert shareholders and institutional investors not to give a negative evaluation just because a company chooses 'to Explain'. In addition, I think we need to ensure that the intention of the Code is widely known among not only institutional investors, but also proxy advisors. Item 12 of the Preamble stipulates "it would not be appropriate ... to conclude automatically that effective corporate governance is not realized by a company on the ground that the company does not comply with some of the principles." Exactly. I think proxy advisors tend to set formal standards, and give negative recommendations to those who do not satisfy them. Instead of doing so, we'd like them to make recommendations by carefully evaluating the content of the explanations. So I think it necessary to well inform proxy advisors of the intention of the Code. Please make consideration on it.

The second request is about the timing of implementation. Concerning the matters to be disclosed according to the Code and the method of disclosure in case of providing explanations, I assume that the TSE will consider how they should be done in the days to come. I think a significant part of such disclosures will be made in the Corporate Governance Reports. At the first general meeting after the implementation of the Code, directors, including independent directors, will be selected. Considering the intention of the Code, I understand that the management, including such independent directors, will consider the application of the Code, as well as how to explain if they choose to Explain instead of Comply. On such an occasion, I suppose that independent directors are expected to have a discussion with sufficient understanding of the company, and make a decision on how to address the Code. So I'd like to request that such a period of time is taken into consideration when setting the timing of filing the Corporate Governance Reports.

The third request is about the revision of the independence criteria. Principle 4.9 stipulates that each company is expected to establish and disclose independence standards concerning independent directors. In doing so, they need to take the TSE's independence criteria into consideration. However, some argue that the TSE's independence criteria set the scope of independence a little too narrow, and it is difficult to select appropriate persons according to the criteria. Many listed companies will need to take certain measures such as securing human resources. The roles of independent directors are to contribute to the company's sustainable growth and the enhancement of medium to long-term corporate value. I think it takes certain time to select qualified candidates. If too much emphasis on the formality results in excessively conservative independence standard, I'm afraid companies will face difficulties due to a narrow scope of qualified candidates. So I'd like to request the TSE to revise the approach to its independence criteria, considering companies' opinions, etc., to match the actual situations. That's all.

[Ikeo, chair] Thank you very much.

Does anybody want to offer an opinion? Mr. Ota, please go ahead.

[Ota, member] As we discussed from the beginning, at the moment, the dominant institutional design among Japanese companies is "Company with *Kansayaku* Board", although I won't repeat the discussion. While there are various arguments from that perspective, I think the draft adequately describes an ideal situation as well as current situation of *kansayaku* system, and I appreciate it.

In this regard, as other members pointed out, there are two approaches which do not necessarily confront each other: one is to find the optimum solution in the current situation taking the reality into account, and another is to try to advance the reform of the current situation based on the philosophy. I suppose that results of these two approaches are not so different. There were different opinions at the starting point, but the secretariat found a common ground in conclusion. This is just my impression.

I have another point to make. Mr. Horie mentioned the exclusion of excessive compliance. I totally agree with him. I think that as an attribute of the Japanese people, we tend to react against expressions in writing, or strict terms or wording. I'm not sure if it is applicable only to the Japanese people, or also in other countries. At least, I think we have such culture.

From this perspective, I'd like to make a request. I have a suggestion for Supplementary Principle 4.1.3 on page 24. As Mr. Yufu explained earlier, the expression was changed from "approve a succession plan for CEO and other top executives" to "engage in the appropriate oversight of succession planning", and it became much easier to understand compared to the initial draft. Yet, considering the English version of the exposure draft to be prepared later, as explained during the first meeting, for instance, the OECD Principles use the expression "planning". In the English translation of the German code, the term "planning" is used. So when the Code is translated into English, the term "planning" would be aligned with general understanding. *[Translator's note: the following argument is over the choice of Japanese word equivalent to "planning" and thus applicable only to the Japanese version].*

Then which word should be used in the Japanese version? As explained earlier, the Japanese word "*keikaku*" (meaning "plan") is associated with a very rigid image: not a few executives may think of something like specifying that candidate A is acceptable, but candidate B is not. Executives would have a strong impression like that. In order to broaden the meaning, we could replace "*keikaku*" with a less strong word such as "*kanngaekata*" (meaning "approach" or "idea") concerning successors. I think it better suits the intention of the principle. I'm aware that it may not be good to talk about the choice of a word at the final stage, but this part bothers me a little. I'd like you to reconsider the wording. That's all.

[Ikeo, chair] Concerning the suggestion for the replacement of the word, if you have any opinions, please voice them now. Certainly, compared with the English word "plan", the Japanese word "*keikaku*" has a narrower or more rigid connotation.

[Ota, member] Probably, top management of companies may be too nervous about that – the appointment or dismissal. If that is not achieved as a result, this statement will be meaningless. Therefore, I think it is desirable to explain what it means is something broader like "*kanngaekata*".

[Ikeo, chair] The word "*kanngaekata*" would, however, be too broad, when compared with "planning".

[Ota, member] However, to translate it in English, it would probably be "planning", considering the example of the OECD Principles.

[Ikeo, chair] I do agree that the word should be translated as "planning" in the English version. Please go ahead.

[Callon, member] I agree with the Chairman, and I also fully understand Mr. Ota's point. There

is no problem with using the word “planning”. The Japanese word “*keikaku*” may have a stronger impression than “plan”. However, “*kangaekata*” is too weak. I’m not sure if we should go for “*keikaku*” or “*houshin* (meaning “policy”)", but the wording should match with the reality. Because a change of CEO is a significant issue for investors, it is critical that companies not only have a concept, approach or idea, but also actually prepare for CEO succession. I think that’s why the codes in other countries reference this issue.

[Ikeo, chair] I think “*houshin*” is the right word in terms of meaning. But we cannot say “oversee *houshin*” in Japanese. So the secretariat suggests that to insert “planning” – English word written in *katakana* – right after “*keikaku*” in a parenthesis.

[Ota, member] I totally agree with Chairman’s idea. I’m usually against the use of English words written in *katakana* more than is necessary, but this suggestion is great.

[Ikeo, chair] Okay, we should go for it.

Mr. Oguchi, please go ahead.

[Oguchi, member] That idea sounds fine, but I think that the Japanese people are already familiar with the English word “planning” written in *katakana*. Then just describing it as “planning” in *katakana* would be simple and clear. I feel such an adscript looks a little too much.

[Ikeo, chair] I’d like to make it an exception of our principle to avoid *katakana* more than is necessary. In this sentence, it should be “*keikaku*” plus “planning” in *katakana* concerning successors. I’d like to modify the wording to “*keikaku* (planning)” to clarify the intention of the principle. Is it all right?

Any other opinions? Okay, Mr. Oba, please go ahead.

[Oba, member] I think this may be the last meeting, so I’d like to share my impressions. This Council took on an unprecedented challenge in some ways. With the efforts of everyone involved, we surmounted many difficulties.

The first point is the speed. In the global community, it has been pointed out that Japan tends to take very long time to do anything, but this draft proposal was prepared in such a short time. Furthermore, it is clearly stated that the Code will come into effect on June 1, 2015, so it dispels concerns of the global community regarding specific timing of implementation. In that sense, we updated the traditional Japanese way.

The second point is the existence of shareholders. I think this is the first principles putting shareholders at the forefront. The Preamble articulates the spirit of the Code in an excellent way, and personally I think General Principles on pages 8 and 9 are extremely important. As these are General Principles, when companies have a doubt about how to address each corporate governance matter, they can come back to these principles. Then they will be able to confirm whether their judgments are appropriate or not.

Principle 1 describes the rights and equal treatment of shareholders. Principle 2 stipulates that companies should always consider the balance among all stakeholders, not just shareholders. Principle 3 concerning disclosure of information is essential. It’s about the issue of transparency of information. Principle 4 describes the responsibilities of directors. I genuinely welcome the use of the term “fiduciary responsibility” here. Principle 5 is about dialogue with shareholders. I believe that this report which puts shareholders at the forefront is very valuable and meaningful.

I'm not just talking about shareholders. I think it will bring about advantageous effects to capital markets, the TSE. The markets which have remained stagnant for 30 years cannot be highly evaluated by the global community. Yet we will be at a significant turning point, and I think this Code will add momentum. I hope this Code will become a driving force of not only corporate management, but also business innovation, in a sense that value creation is the starting point of everything, involving institutional investors. That's all.

[Ikeo, chair] Thank you very much.

Anybody else? Mr. Takei, please go ahead.

[Takei, member] Yes, as other members already mentioned, I think this is a great proposal drafted as a part of the economic growth strategy in such a short time constraint, with the "all Japan" efforts. I would also like to express my gratitude and respect to the secretariat members who organized diverse opinions. I suppose they worked on this difficult task all day long. Thank you very much.

Earlier, a member referred to Legal department. I think I should make a comment on it. Certainly, whenever the Government issues this kind of guidelines, companies tend to think "Legal department should examine first". However, this Code takes the principles-based approach, so companies should address the Code based on the fundamental aim of the Code upon understanding for what purposes each item of the Code is written. While legal department will help the management understand the aim and rationale behind each principle of the Code, other departments may well be involved in the preparation for the Code. While the member mentioned that the top management including CEO should take a lead, I think all teams in a company – all departments such as Corporate Planning, IR, Finance and Accounting, and CSR – should work on it as a cross-functional team in an organized form. The team work is preferred.

Unless they consider the intention of why each item of the Code is described, they cannot even describe their compliance or explanation. They should properly understand a big picture of the Code first, and then take necessary actions. They should not leave everything to Legal department. Although I am a lawyer, I really think so.

In this connection, I really think the Preamble is very well-written. In the earlier meeting, Chairman said "the Preamble should be written in the end" and the Chairman's policy actually went well. The Preamble articulates all necessary matters about the aim, background and meaning of the Code in a well-organized and easy-to-understand manner. To interpret the Corporate Governance Code, I'd like to recommend that users carefully read every single sentence of the Preamble first, and then read the Code. I think the Preamble is that much excellent: there is no omission of necessary matters, and the intention is well-articulated.

Especially, I take much notice to Items 7 and 8. Item 7 describes "growth-oriented governance": this is required for decisive decision-making, while defensive governance is also important. As shown in Item 8, the Code promotes medium to long-term investment. It means that medium to long-term investors are important partners for companies. While we can see such progresses as the Pension Reform and JPX-Nikkei 400, I consider it important as the governance being an environment to accept such medium to long-term risk money.

When it comes to governance, most explanations conventionally focus on defensive



governance, so the explanation of “growth-oriented governance” is much newer than such conventional explanations, and excellent explanation of governance, integrating various matters like an Integrated Report. For companies aiming at achieving sustainable growth, it offers good guidance. I’d like various people to thoroughly read the Preamble and understand the intention of each sentence first. Then I’d like them to read each principle of the Code, understand the intention of each Principle and Supplementary Principle, and consider measures to address these principles. That’s all.

[Ikeo, chair] Thank you very much.

Professor Kanda, would you like to share your thought?

[Kanda, member] Thank you, I’d like to briefly make comments. As other members already mentioned, I’d like to express my appreciation for tremendous efforts of Chairman and the secretariat members who compiled the draft.

I’d like to mention two things about what I felt about the members’ comments. The first point overlaps with what Mr. Takei just mentioned. I hope that listed companies will not leave everything solely to legal or compliance departments. Hopefully, the Code should be worked on by the management and planning division.

The second point is about English translation of the Code – the draft at the moment. I hope it will be translated in a way to clarify the intention, by avoiding literal translation and using ingenuity. The Code contains many difficult Japanese expressions. So when preparing an English version, please exercise ingenuity and ensure that the intention is clearly communicated. Thank you very much.

[Ikeo, chair] Please go ahead.

[Callon, member] As Pf. Kanda indicated, the English translation is very important. If needed, I would be more than happy to help.

I believe that the establishment of this Code represents revolutionary progress. As Mr. Oguchi indicated earlier, from the perspective of “growth-oriented governance”, the Code will enable Japan to make a quantum leap to become a leading country in corporate governance. I really appreciate the efforts of all the secretariat members, the Chairman, and all of the members of the Council.

I thought it would be better to make my comments after listening to the opinions of other members who have profound expertise and experience. I agree with what Mr. Oba said about the speed of drafting the Code. There is a Japanese expression “big company disease”. Similarly, there may be such a thing as “big economy disease” as well. Because of Japan’s lost two decades, the international community may believe that Japan is suffering from some such disease. However, the content of this Code as well as the speed of drafting the Code can be viewed as Japan’s counter-argument. Please allow me to use the term “our country,” because I’m Japanese in my heart. I think that our country’s energy, our country’s power, and our country’s excellence are fully demonstrated in this Code.

As Mr. Toyama indicated, this past year saw various corporate governance initiatives, from the JPX-Nikkei 400 and the Ito Review to the Stewardship Code as well as the Corporate Governance Code. This is the inaugural year for Japanese “growth-oriented governance”, which supports Japanese companies managing for value creation and growth-oriented business management. We now beginning the process of soliciting public

comment, and I think we can anticipate positive responses.

Unfortunately, global investors have come to view Japan's corporate governance as poor governance. However, this Code covers not only the number of independent directors, on which we have had intensive discussion, but also directors' fiduciary responsibility, the roles and responsibilities of directors, the importance of dialogue with shareholders, director training, along with other reforms. This single Code comprehensively contains all of these matters, and the comprehensiveness is essential. This is a revolutionary leap forward, and I'd like to express my gratitude to everyone present. With respect to the implementation of the Code, considering the nature of the Code as well as the seriousness and purposefulness of Japanese companies, I believe we will see very good outcomes from this Code. My apologies for the long comment. Thank you very much.

[Ikeo, chair] Thank you very much. We are good at catching up [with others].

I think everyone has already made their comments. Are there any additional comments? If not, I'd like to close the discussion.

Today, the members pointed out the significance of the Code, the need to make the Code widely known, and some issues concerning the implementation. On the premise that there are such opinions, and upon changing one word as per we agreed, I declare that the draft of the Code was agreed upon. Thank you very much.

However, there could be minor modifications of the wording to ensure the consistency of expressions or just change postpositions. In this regard, please leave such matters to my discretion.

(Members said "no objection.")

[Ikeo, chair] Thank you very much.

As mentioned earlier, we will call for public comments on the draft. I'd like to ask the secretariat to explain the procedures.

[Yufu] Concerning the draft of the Code, we plan to call for public comments in Japanese and English. I think the English version will be published later than the Japanese version due to time required for translation, but we hope to prepare it as soon as possible.

In doing so, we would like to regard that the original is the Japanese version, and the English version is just a provisional translation prepared by the secretariat – the Financial Services Agency and the TSE. In preparing an English translation, we will make efforts to reflect opinions expressed at this Council of Experts as much as possible. However, as Mr. Kanda pointed out, in some cases, please understand that we will place a priority on communicating the intention in an easy-to-understand manner by free translation. As for a plan for successors, we probably translate it as "succession planning".

As for the deadline for submission of public comments, we assume it will be open for comments for approximately 1 month from the publication.

[Ikeo, chair] Thank you very much. After soliciting public comments, in response to such comments, I'd like you to attend another meeting to finalize the Council of Experts' "the key elements of the Corporate Governance Code", or the proposal of the Code.

So far, we have met 8 times. Thank you very much for taking your time from your busy schedule. I'm not sure why I was appointed as Chairman. I accepted the request without due consideration as usual. Yet as I considered various things after the acceptance, I got anxious

about a downside risk: while drafting the Corporate Governance Code increasingly draws the attention of both local and international communities, whatever the content will be only criticized. So far it seems a groundless fear, and we could complete the draft, which is likely to receive favorable responses. This is achieved thanks to the cooperation of the members as well as the competent ability of the secretariat. I really appreciate it.

We had active discussion on corporate governance from a broad range of perspectives. We had very meaningful Council meetings, and I learnt a lot from this Council. Again, I'd like to thank all of you.

Finally, I'd like to ask the secretariat to make necessary administrative announcements, if any.

[Yufu] As Chairman just mentioned, the next meeting of the Council will be held one more time, maybe around February. We will inform you the details later. Thank you in advance for your cooperation.

[Ikeo, chair] Thank you. Now I declare today's Council closed. Thank you very much for your cooperation.

End