

Minutes of the 6th Council of Experts Concerning the Japanese Version of the Stewardship Code

1. Time and date: 4:00–5:30 pm, February 26 (Wednesday), 2014
2. Place: Financial Services Agency

[Kansaku, Chairman] Let us start the 6th Meeting of the Council of Experts Concerning the Japanese Version of the Stewardship Code (the Council).

The preliminary draft of the Japan’s Stewardship Code (the Code) completed at the last council meeting was published as an exposure draft for public comments in both Japanese and English. As a result, we received comments in Japanese from 26 individuals/entities and 19 in English.

Today, the secretariat will present an overview of the received public comments/opinions and proposed responses. The secretariat will then present a revised draft of the Code in both Japanese and English based on the results of the public comments. This will be followed by free discussion among council members, based on which we would like to finalize the Code. Promptly after the closing of today’s meeting, an overview of the received public comments/opinions and the responses to such comments/opinions will be published, together with the final version of the Code. Please note that we received a considerable number of comments/opinions, but the material distributed today includes only the major comments. We also plan to publish our response to those excluded from today’s material on the FSA’s website later.

Reflecting the comments addressed at the 4th Council Meeting in response to the secretariat’s explanation of issues associated with Japan’s existing legal framework, the secretariat has prepared a document containing additional interpretation to clarify the legal issues associated with the development of the Code. Although we will leave out specific explanation due to limited time, please note that the document is distributed as reference material for today’s meeting, and is scheduled to be published on the FSA’s website together with the publication of the final version of the Code.

Let’s start with the secretariat’s explanation.

[Yufu] I would like to start with Material 1.

Refer to Materials 1-3

Lastly, I will refer to the revisions of the draft Code.

We have revised the upper part of Page 2. Relevant developments following the public comments were added to the paragraph. Next, we are considering inserting a Footnote 2 at the end of paragraph 5 of the Preamble stating, “In addition, the Code does not preclude a decision to sell a holding, where this is considered in the interest of clients and beneficiaries.” This expression is identical with the U.K. Stewardship Code.

We also suggest inserting a Footnote 3 at the end of paragraph 6 of the Preamble in relation to the clarification of the legal interpretation as stated earlier.

Footnote 4 was added to the fourth line of Guidance 1-1 to provide a definition of “purposeful dialogue” in response to the opinion that addressed the needs for clarification of ‘purposes’.

Next, I will talk about Principle 2. We are considering moving the phrase ‘put the interest of their client and beneficiary first’ in Guidance 2-2 in the preliminary draft to the beginning of Guidance 2-1, thereby

changing the structure of the paragraph by first stating that “institutional investors should put the interest of their client and beneficiary first” then noting that at times investors inevitably face the issue of conflicts of interest.

Next, Principle 3. We are considering inserting the statement, “When investors monitor investee companies, a variety of factors, including non-financial ones, may be considered as relevant” in the first line of Guidance 3-3.

We added Footnote 6 to the phrase ‘an understanding in common’ in the first line of Guidance 4-1 stating that “the effort to arrive at an understanding in common may result in an agreement to disagree, but may provide a better understanding on why they disagree”.

The addition to Guidance 4-3 relates to Footnote 10, which was intended to note that in receiving information on undisclosed material facts due to a special relationship with an investee company, institutional investors should take measures to stay in compliance with insider trading regulations. No addition or revision was made to Footnote 10 itself, but we added a sentence to Guidance 4-3 stating, “In principle, institutional investors can well have constructive dialogue with investee companies based on public information without receiving information on undisclosed material facts.”

[Eguchi, member] Not a question, but I would like to comment for reporting purposes. Guidance 7-3 under Principle 7 states that “exchanging views with other investors and having a forum for the purpose may help institutional investors engage better with investee companies and make better judgments.” In this regard, I would like to report that we as a collection of individuals engaged or affiliated with investment activity plan to launch an initiative, in cooperation with the Ministry of Economy, Trade and Industry (METI), that will consider the desirable form of the said forum for exchange of views, as well as the items that are to be discussed at such a forum.

[Kansaku] Thank you.

I would also like to share information with council members. The general meeting of the Financial System Council was held on February 24, 2014, and Mr. Yufu presented the progress of discussion and an overview of the preliminary draft “Principles for Responsible Institutional Investors,” which was approved at the Stewardship Council meeting on December 26, 2013.

At the general meeting, we received comments and opinions from a number of members of the Financial System Council, which were basically favorable to the draft of the Code. Some questions were asked, for example, in relation to the consideration of non-financial factors such as environmental issues and sustainable investment under the Code. Another question is related to the relationship between fiduciary duties and stewardship responsibilities, especially the significance of the responsibilities of institutional investors. There was an opinion suggesting development of a framework to give a positive assessment to the investor who is vigorously taking a ‘comply or explain’ approach under the Code. Given opinions and questions from a number of members, I felt a high level of interest among them towards stewardship.

[Yufu] I would like to report on one more issue.

The Code requests the FSA to publish the list of institutional investors who announce their acceptance of the Code. I would like to explain the method of the publication of the list currently considered by the FSA. Details will be available on the FSA’s website, but I would like to note that the FSA is currently considering requiring investors, in addition to disclosing their acceptance of the Code, to set out guidelines for implementing the Code, including three policies for advance disclosure. Although it is highly possible that institutional investors choose not to comply with some of the principles and explain why they are not complied with, we are basically assuming that the FSA will publish the list of

institutional investors after they disclose their intention to accept the Code as well as the three policies and notify the FSA

On top of that, the FSA assumes a quarterly update of the list. Specifically, avoiding the end of each quarter which is generally busy, the FSA sets the deadline for notification at the end of February, May, August and November, and will update the information in following month. It should be noted that initial publication of the list, which covers institutional investors notifying their intention to the FSA by the end of May 2014, is scheduled for early June 2014.

There is fairly limited time left until the initial list disclosure, and June is the busiest season for persons having charge on the general shareholders meeting. In order to promote acceptance of the Code by a wide range of institutional investors, the FSA will, for the initial disclosure only, accept institutional investors who publicly disclose their intention to accept the Code first and delay the timing of disclosure for the other required items, such as the policies for disclosure, until the next update.

[Hamaguchi, member] When investors approach investee companies for dialogue, they may face a number of rejections from investee companies. What actions should the investors take in the event their request is declined? I wonder if it is possible to have a framework in place where investors disclose the name of the company that declined their request for dialogue or report to the FSA. Some of the U.S. pension funds do this, which is quite sensational. As I mentioned previously, meaningful dialogue is always possible with investee companies that are willing to do so. Such companies would normally maintain a solid ROE. The issue is about companies that are not willing to dialogue. Are there any views on this?

[Yufu] It is a difficult issue. However, as noted at the beginning of this meeting, issuer companies should change their mindset; for example, the automatic assumption of a negative view by the investor upon receiving the request for dialogue. Dialogue must be interactive between investee companies and institutional investors. The very purpose of the Code is to promote sustainable growth from a medium to long-term perspective; thus investee companies should essentially welcome the opportunity to dialogue. In fact, some issuer companies support such idea. Going forward, we will strive to promote understanding by the investee companies.

[Kansaku] Thank you for your comments.

I assume that all council members consent to the draft response to the public comments and revised draft of the Code presented today. We will finalize these drafts accordingly. Thank you very much.

Lastly, Mr. Kuwabara, Director-General of the Planning and Coordination Bureau, will make closing remarks.

[Kuwabara] I very much appreciate the active and in-depth discussions by council members throughout the six meetings held to date.

As you know, Japan's Stewardship Code is positioned as part of Japan's growth strategy or the third arrow of Abenomics. At the January 2014 Davos meeting, in his keynote speech Prime Minister Abe referred to the formulation of the Code. Expectations for the Code are rising substantially not only within Japan but also overseas. As noted earlier, about 40% of the public comments were from overseas, all of which were supportive of the Code's development. We recognized again the high level of interest in the Code and its significance. Looking ahead, it is expected that as Japan's Stewardship Code becomes widely accepted, overseas investors' views of the Japanese equity market will improve and thereby not only short-term but also medium- to long-term investment will increase, resulting in further prosperity for Japan's equity market.

Based on the finalization of the draft, as the secretariat of the Council, we will strive to promote acceptance of Japan's Stewardship Code by as many institutional investors as possible through public relations activities such as seminars for domestic and overseas institutional investors.

The solid foundation for stewardship is complete, and we are facing an important phase of preparing for implementation. Further, the Code requires periodic review of itself. Again, I appreciate the active discussions that have taken place so far between council members and I would like to end my speech by asking for your continuing support and cooperation in the future. Thank you very much.

[Kansaku] The Council has met six times since August 6, 2013, and has reached a milestone today. I highly appreciate the council members' participation and vigorous discussions despite their busy schedules.

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