Minutes of the 7th Council of Experts Concerning the Corporate Governance Code

1. Time and date: 4:30–6:30 pm, November 25 (Tuesday), 2014
2. Place: Financial Services Agency

[Ikeo, Chairman] Although it is a few minutes before the scheduled opening time, as all the prospective attendees are here, I'd like to open the seventh Council of Experts Concerning the Corporate Governance Code. Thank you very much for taking time out of your busy schedule for the Council.

I would like to start the proceedings. The material for today is the revised working draft. The secretariat revised the initial working draft by reflecting our discussion at the last meeting, and added new descriptions pertaining to two parts. The first part is in Chapter 1 "Securing the Rights and Equal Treatment of Shareholders", specifically, Principle 1.4 so-called cross-shareholdings on page 4. The second part is in Chapter 4 "Responsibilities of the Board", concerning the composition, institutional designs, procedures, etc.

As usual, the secretariat will be explaining the working draft first, and then we will be discussing it.

Now I'd like to hand it over to the secretariat for the explanation of the working draft in today's Material.

[Yufu, Director of the Corporate Accounting and Disclosure Division] I'll be explaining the material in a vertical format in black and red fonts at your hands.

As it is written on the front cover as "Excluding the Preamble", if you flip a page, you will see the letter P in a circle, meaning that this part - the preamble - is still pending. We plan to prepare a draft preamble for your consultation at the next meeting.

Please flip another page. General Principles are quoted on these two facing pages. In response to your comments at the last meeting, we rewrote the sentences by avoiding the use of the expressions "etc." and "such", and also replaced English words written in *katakana* with equivalent Japanese words, where possible. Furthermore, as for the wordings which vaguely referred to "the board and the *kansayaku* board", we made efforts to clearly distinguish *kansayaku* and the *kansayaku* board. We made these changes throughout the draft, so I will not refer to them in my explanation any more.

On these two facing pages, we deleted the first line which was like a note stating "to achieve sustainable corporate growth…" for the editing purpose, because the same expression is used in General Principle 5.

Furthermore, we added a title to each General Principle within the box. As for General Principle 1, we used to have the title "Respecting Shareholders' Rights". Taking your opinions into account, we changed the title of Chapter 1 to "Securing the Rights and Equal Treatment of Shareholders". And considering the intention of this change, we made several accompanying revisions such as changing the expressions in the Notes to "take appropriate measures to fully secure shareholder rights".

The next revision is made to General Principle 2. In the last meeting, it was pointed out that a better expression than "smooth cooperation with stakeholders" should be considered. In response, we rephrased it as "appropriate cooperation".

Regarding General Principle 4, two inputs were obtained from you. The first input was that accountability should be stated on a higher level. Another one was concerning item (2) of General Principle 4: it was difficult to understand the intent of "ensuring accountability" written in a parenthesis. Based on these inputs, we revised the first sentence of General Principle 4 in a way to refer to accountability appropriately.

Furthermore, right above items (1) to (3), we changed the expression from "roles and functions" to "roles and responsibilities". It was pointed out that the expression "functions" is insufficient, so we changed this part to "roles and responsibilities".

Now I'm moving on to specific principles. Please take a look at pages 1 and 2. The changes here are mainly rhetorical, such as clarification of "etc." We also changed the order [of Supplementary Principles]. There are no more substantial changes, so let me move on to pages 3 and 4.

Previously, Supplementary Principle 1.2.1 was described with the expression "information pertaining to the general shareholder meetings". It was pointed out that if it means a broad range of information relevant to the general shareholder meetings, it should be written in a way readers can understand what it means. So we modified this part to read "(c)ompanies should provide accurate information to shareholders as necessary in order to facilitate appropriate decision-making at general shareholder meetings."

Following that, Supplementary Principle 1.2.2 is pertaining to early dispatch of the convening notice. As it does not mean to simply encourage early dispatch of any information, we limited the content by adding "while securing the accuracy of content".

Please look at the second paragraph from the bottom of page 3. As written in the *[Background]*, we heard various opinions concerning the general shareholder meeting in this Council. In addition to such opinions, we added some descriptions related to exceptional events where consistency with other existing systems may need to be considered.

Please look at Supplementary Principle 1.2.5 on page 4 on the right. It refers to institutional investors who hold shares in the name of a trust bank or other party. Previously, it concluded "should allow their participation." We revised this part as it was pointed out by the members that the issue would generally be solved by the proxy system, although we still need to examine practical aspects. Let me read it out: "In order to prepare for cases where institutional investors who hold shares in street name express an interest in advance of the general shareholder meeting in attending the general shareholder meeting or exercising voting rights, companies should work with the trust bank (*shintaku ginko*) and/or custodial institutions to consider such possibility." In this way, we modified the statement from the previous version which definitively concluded that their participation should be allowed.

Let me read out Principle 1.4. Under the caption "Cross-Shareholdings", it reads "(w)hen companies hold shares of other listed companies as cross-shareholdings, they should disclose their policy with respect to doing so. In addition, the board should examine the mid- to long-term economic rationale and future outlook of major cross-shareholdings on an annual basis, taking into consideration both associated risks and returns. The annual

examination should result in the board's detailed explanation of the objective and rationale behind cross-shareholdings. Companies should establish and disclose standards with respect to the voting rights as to their cross-shareholdings."

I'll skip a few pages. Please turn to page 7. Page 7 is about relationship with stakeholders other than shareholders. During the last meeting, it was pointed out that [Section 2] should not begin with the specific principles such as the ethical standard or code of conduct, and that it would be better to describe the establishment of stakeholder-conscious business principles first, and then discuss particulars. Accordingly, we added what is currently described as Principle 2-1.

Next, please take a look at page 10. Under Principle 3.1, items are listed up from (i) to (v). Item (v) clarifies that they should disclose reasons for appointing each individual based on policies and procedures developed and disclosed pursuant to Item (iv).

Concerning 3.2.1 on the same page, previously it was written as "the board and the *kansayaku* board" without distinguishing them. Now, considering the intent of the revised Companies Act, we clarified who should take which steps. 3.2.1 describes the steps to be taken by the *kansayaku* board, and newly-added 3.2.2 describes the steps to be taken by both the board and the *kansayaku* board. We just clarified who should take these steps and the steps themselves remain unchanged from the previous version.

I'm moving on to page 12, "Responsibilities of the Board". This time, we added the "Notes" which was pending at the previous meeting. The content is roughly divided into two parts. In the first paragraph, it is written that the Companies Act of Japan stipulates three alternatives for institutional designs; and as for Company with Three Committees (Nomination, Audit and Remuneration) and Company with Audit and Supervisory Committee, other countries have similar types of companies where committees are established [under the board] to perform certain roles. On the other hand, because Company with *Kansayaku* Board is a Japan-specific system, we added some explanations of it. Then we concluded "(i)rrespective of which form of organizational structure is adopted, what is important is that the various institutions within the company effectively and fully execute their responsibilities through creativity and ingenuity." This is the first paragraph.

The second paragraph was written, considering that this Code is supposed to be drafted as part of the growth strategy in the first place, and the members of the Council continually expressed opinions concerning "growth-oriented governance". Generally speaking, business judgements may cause damage to the company and/or others. In such a case, there is a possibility that the management and directors are personally held liable for the damage. Concerning whether or not they are actually held personally liable, according to legal precedents, it seems the existence of liability is judged often by focusing on whether or not the decision-making process at the time in question was rational. Here, based on the said assumption, we wrote at the upper part of page 13: "The Code (draft proposal) includes principles and practices that are expected to contribute to such a reasonable decision-making process, and promote transparency, fairness, timeliness and decisiveness as well."

In the US and Europe, it is said there are business judgment rules under the case laws. Of course, we cannot write "there will be no problem regarding business judgements made in accordance with the Code." But still, recognizing such limitation, we attempted to provide

possible solution in the Notes.

As for Principle 4.1 on page 13, we replaced the word “functions” with “roles and responsibilities”.

Below that, concerning Supplementary Principle 4.1.2, it was pointed out that it is unreasonable to require a commitment to a long-term plan, such as 10-year plan, so we limited this part only to mid-term business plan.

Please look at the box at the bottom of page 13. Previously, we referred to “ensuring accountability” in a parenthesis, and the members pointed out that it is difficult to understand the intention. So we rephrased this part so that readers can understand what it means. Specifically, please look at Principle 4.2. The board should view the development of an environment which supports risk-taking as one of its main roles and responsibilities, and should welcome proposals from the management based on healthy entrepreneurship. And with the aim of securing accountability, it should fully examine the proposals from various angles. Furthermore, when approved proposals are implemented, it should support timely and decisive decision-making of senior management.

As for 4.2.1 on page 14, in response to your opinion that the proportion of cash remuneration and equity-based remuneration is very important, we added a statement to that effect.

As for the third line of 4.3, we reconsidered what should be mentioned in the box, and what should be mentioned in the following Supplementary Principles. As it was pointed out that such an expression as “should appropriately… reflect the evaluation in its assessment of the senior management” would be appropriate in the box, we modified this line accordingly. In the meantime, as some specific descriptions are deleted from the statement in the box, we referred to the removal of the management in Supplementary Principle 4.3.1 instead.

As for 4.4, we changed the expression from “*kansayaku* (board)” to “*kansayaku* and the *kansayaku* board”.

Please turn to page 15. There are some modifications in the box on top of the page. This is concerning ‘defensive functions’ of *kansayaku* and the *kansayaku* board. Previously, it sounded as if they should do this and that “to fulfill defensive functions”. However, based on the opinion that their functions are not limited to ‘defensive functions’, we edited the sentence accordingly.

As for Supplementary Principle 4.4.1, taking your comments into account, the last sentence was revised: “the *kansayaku* board should secure cooperation with outside directors”.

The principles hereinafter are newly added this time. First, Principle 4.5 is about “Fiduciary Responsibility of Directors and *Kansayaku*”, and states that they should keep in mind their fiduciary responsibilities to shareholders, “secure the appropriate cooperation with stakeholders and act in the interest of the company and the common interests of its shareholders.”

4.6 is about “Business Execution and Oversight of the Management”. In the second line, it states “companies should consider utilizing directors who are neither involved in business execution nor have close ties with the management.” We included this principle as a bridge before discussing independent directors in 4.7, and described the relationship between the

oversight of management and execution of operations.

Then Principle 4.7 is titled as “Roles and Responsibilities of Independent Directors” and four items are listed: (i) advisory role; (ii) monitoring of management; (iii) monitoring of conflict of interest; and (iv) representing the views of minority shareholders and other stakeholders.

Principle 4.8 on page 16 is titled as “Effective Use of Independent Directors”. Let me read it out: “Independent directors should fulfill their roles and responsibilities with the aim of contributing to sustainable growth of companies and increasing corporate value over the mid- to long-term. Companies should therefore appoint at least two independent directors that sufficiently have such qualities. Irrespective of the above, if a company in its own judgement believes it needs to appoint at least one-third of directors as independent directors based on a broad consideration of factors such as the industry, company size, business characteristics, organizational structure and circumstances surrounding the company, it should disclose a roadmap for doing so.”

In the *[Background]*, we first wrote that it is not appropriate to consider that the companies can achieve corporate growth simply by appointing independent directors. Then, it continues that the important factor is whether the companies can take appropriate measures to make use of independent directors. The last two lines conclude by explaining that the draft Code specifies that at least two independent directors should be appointed as having multiple independent directors will significantly enhance the possibility of their presence being fully leveraged, in a sense that they will not be isolated in the board.

Supplementary Principle 4.8.1 is also a norm to make the best use of independent directors. Please take a look at the second line. Independent directors should endeavor to exchange information and develop a shared awareness among themselves from an independent and objective standpoint, for instance, by holding regular meetings, which include so-called executive sessions, consisting solely of independent outside members.

In the following *[Background]*, it explains that meetings of independent outside members can consist solely of independent directors or can also include independent *kansayaku*.

4.8.2 is about a lead independent director or senior independent director. It describes that independent directors should work on establishing a framework for the coordination with the management and cooperation with the *kansayaku* board, for instance, by electing a lead independent director by mutual vote.

As for 4.9, I understand that this issue was not so controversial in this Council, but we’d like to confirm some factual situations for administrative purpose. Therefore, this principle is still pending at this point. We plan to present it for the next meeting.

4.10 is titled as “Use of Optional Approach” on page 17. Please look at the box of 4.10. In the second line, it is written that “companies should employ optional approaches, as necessary, to further enhance governance functions.” 4.10.1 states, from the third line, that “in order to strengthen the independence, objectivity and accountability of board functions on the matters of nomination and remuneration of the senior management and directors, the company should seek appropriate involvement and advice from independent directors in the examination of such important matters as nominations and remuneration by, for example,

establishing optional advisory committees under the board to which independent directors make significant contributions."

In the corresponding *[Background]*, the last sentence, which begins with "in such cases", states that if the companies establish optional committees concerning the nomination and/or remunerations, such committees are not necessarily named as nomination committee and/or compensation committee. It could be one committee which addresses various governance functions, including the design of corporate governance such as related-party transactions or nomination of *kansayaku.* This is about an optional committee or committees, and thus we wrote that there are various ways to set up such committees.

The first sentence of 4.11 is about the board. First, it states that the board as a whole should be well balanced in knowledge, experience and skills, and the board should secure both diversity and a suitable size.

The second sentence is about *kansayaku.* It states that at least one person who has appropriate knowledge in finance and accounting should be appointed.

Following that, it states that the board "should endeavor to improve its function" by analyzing and evaluating the board as a whole.

Now I'm moving on to the right, page 18. Supplementary Principle 4.11.1 states that the board should formulate and disclose their approach for ensuring an appropriate balance of knowledge and other competence of the board as a whole, diversity and appropriate boardsize.

4.11.2 states that directors and *kansayaku* should devote reasonable time and effort, and in case they concurrently serve as officers at other listed companies, the number of such positions should be limited to a reasonable level. Furthermore, it states such positions should be "disclosed each year".

4.11.3 "the board should analyze and evaluate its effectiveness as a whole, taking into consideration the relevant matters, including the self-evaluations of each director". As we thought the idea of publishing the complete results may be difficult, we wrote that the board should disclose a summary of the results.

4.12 describes a climate enabling open-minded discussion.

4.13 on page 18 is titled as "Information Gathering and Support Structure". It states "directors and *kansayaku* should proactively collect information, and as necessary, request the company to provide them with additional information."

It continues to page 19. "Also, companies should establish a support structure for directors and kansayaku, including providing sufficient staff." Then, "the board and the kansayaku board should verify whether information requested by directors and kansayaku is provided smoothly."

4.13.1 describes information gathering by directors and *kansayaku* separately.

4.13.2 states that they [i.e. directors and *kansayaku*] should consider consulting with external specialists at company expense "where they deem it necessary".

4.13.3 refers to coordination among the internal audit department, directors and *kansayaku.* Starting from "in addition", the second line describes the necessity of arrangement to provide information adequately to outside directors and *kansayaku*, including an appointment of an individual who is responsible for communicating and

handling requests within the company such that the requests for information about the company by outside directors and outside *kansayaku* are appropriately processed.

4.14 is about "Director and *Kansayaku* Training". The first sentence in the box clarifies that directors and *kansayaku* should make efforts for self-development. Then it continues that companies should provide training opportunities to support their efforts.

4.14.1 describes training when they assume their office, as well as continuous training after they have assumed their office.

4.14.2 is about disclosure of training policies.

Finally, please turn to page 21. Please look at Supplementary Principle 5.1.3. We used to use the expression "identify beneficial owners" here. However, because shareholders, in general, legislatively mean nominal shareholders in Japan, it was pointed out that the term "beneficial owners" may contradict with such legislation and the scope of such term is uncertain, and thus we should avoid the use of the term. Accordingly, we rephrased it as "companies should endeavor to identify their shareholder ownership structure." Furthermore, concerning shareholders' response, we changed the wording from "anticipated to cooperate" to the stronger expression: "It is desirable for shareholders to cooperate".

That's all for my quick explanation.

[Ikeo, Chairman] Thank you very much.

Now I'd like to open a free discussion. Mr. Toyama is absent today, but he submitted his opinion paper, which is distributed to all of you. Mr. Mori, who is here, also submitted his opinion paper, which is also distributed to you. The secretariat already sent them to the members in advance – although Mr. Mori's paper was sent at the last minute – I will not read them out. However, please take them into account for the discussion.

Concerning how we proceed with the discussion, I'd like to divide the discussion into two parts again.

In the first half, we will discuss institutional designs under "Responsibilities of the Board" from page 15 to page 19. In the second half, we will discuss the remaining parts from page 1 to page 14, as well as pages 20-21, including the revisions made in response to your inputs in the last meeting. I'd appreciate your understanding and cooperation.

Now I'd like to hear your opinions on institutional designs and other points stated from page 15 to page19. Who would like to start? By the way, Notes are newly added on page 12, and it is related to the discussion in the first part. So please include page 12 in the discussion of the first part.

Mr. Ota, please go ahead.

[Ota, member] Concerning Principle 4.8 on page 16, I'd like to ask a question for clarification, and then make a comment.

Including 4.8, all sentences describe "listed companies" as a target to follow the principles. I think we discussed it at the second or third council. Someone asked a question about the scope of all listed companies, and the answer was all of them.

My first concern is the scope of listed companies, when they include companies listed on various emerging markets. I'd like to confirm the scope of listed companies defined by the secretariat first, and proceed to further discussion.

[Ikeo, Chairman] I'm handing it over to the secretariat.

[Yufu, Director of the Corporate Accounting and Disclosure Division] We basically plan to specify the applicable companies in the Preamble. So I'd like you to discuss it at the next meeting.

With that being said, when we write "listed companies" here, we are under the assumption that the term at least includes companies listed on the Main Markets, namely TSE First Section and Second Section. That's the assumption of the secretariat.

Nonetheless, I'd like to hear various opinions from the members next time.

[Ota, member] I see. Actually, I requested TSE to provide data. Looking at the listed companies in Japan by listing market, 96% of total market cap is made up by the companies listed on the First Section. I believe that it is necessary to clarify that the entire Code provides General Principles which should be complied with by all listed companies, in other words, all companies listed on all markets including emerging markets; and also make realistic consideration of the applicable scope of Supplementary Principles.

Stated another way, the purpose is to avoid the situation where the Code loses substance because of formalistic or superficial compliance.

Specifically speaking, although I'm aware that this should be discussed in the next meeting, the draft proposal is written in a way to facilitates appointment of multiple independent directors. So as for the applicable scope of the Code, due to the said circumstances, I'd like to suggest that we should consider segment-by-segment application, for instance, by limiting the scope to the companies listed on the First Section or companies in JPX-Nikkei Index 400. This is my first proposal.

In this connection, let me tell you why I made such a proposal. While we say all listed companies, there are approx. 3,400 listed companies. And in case of promoting appointment of multiple independent directors, the biggest challenge would be securing the number and quality of such directors. If we limit the applicable scope to the companies listed on the First Section, there are approx. 1,800 companies which need to have multiple independent directors. Suppose approx. 700 companies currently do not have any independent director, and approx. 720 companies have only one independent director. Even if we limit the applicable scope for appointing multiple independent directors to the First Section companies, it will be necessary to additionally secure approx. 2,100 persons. Beyond that, if we encourage all listed companies to appoint multiple independent directors, it requires approx.4,800 persons for such new positions. I'm wondering if this is truly realistic.

So here is my second suggestion. The first suggestion was to focus the applicable scope, and for that purpose, I think there would be two measures to be taken. While we have been discussing it under the assumption that the Code should be implemented before the general meetings next June, we should either set a certain transition period, or start preparation for enabling companies to secure a large number of independent directors at once. Specifically, relevant organizations and government agencies should work together to consider a mechanism enabling the utilization of a broad range of deserving human resources, and properly establish an information center which prepares and uses human resources data by securing the fairness and transparency.

At least, in the proposal by the Council of Expert, I believe we should propose that such preparation is required for practically facilitating the appointment of multiple independent

directors.

For your information, Japan Audit & Supervisory Board Members Association (JASBA), a public interest incorporated association, has a talent bank system, and more than 600 individuals registered with the bank. To make the best use of their knowledge, it has the talent database. There is a system to supply human resources for outside officers, where upon requests or inquiries from companies, a certain number of registrants undergo interviews and negotiations, and assume new positions every year. This service is, of course, free of charge. JASBA has already established a mechanism enabling rotations of a certain number of human resources for not only *kansayaku,* but also directors. I'd like to propose the establishment of a public, not-for-profit information center, including the use of such a database.

May I continue?

[Ikeo, Chairman] Sure.

[Ota, member] Let me briefly make a comment on Supplementary Principle 4.11.2 on page 18. Reflecting our discussion in the past, it contains the description which limits the number of concurrent positions of outside officers. I support it.

In the meantime, however, from the perspective of maintaining the independence, I think it is desirable to limit not only the number of concurrent positions, but also the term of office as some members pointed out before. At the moment, I won't specifically suggest how many years their term of office should be, or up to how many companies they could serve, but I think we should have a balanced discussion.

That's all for now.

[Ikeo, Chairman] Thank you very much.

Any other comments? Please do not hesitate. Mr. Oguchi will speak first.

[Oguchi, member] Thank you. I appreciate that the secretariat wrote a broad range of important matters throughout the Code.

My first point is related to what Mr. Ota just mentioned. It may apply to the entire Code. While [companies] have to do various things upon establishment of this Code, I think they naturally need a bridge between the current situation and the ideal situation or best practice. In my understanding, it would be better to write about it comprehensively in the Preamble. Principles are Principles, but I personally think that the Preamble should be written, taking the reality into account. This is my first point.

I have another point. Although I'm comfortable with the working draft as a whole, there was one point, with which I'm not comfortable. It's 4.10.1 on page 17. In my understanding… at first, I understood that in case independent directors compose the majority of the board, an objective and independent system will be secured; and in case they do not compose the majority, committees will supplement the gap. Then the fourth line of 4.10.1 describes – with "for instance" – "[optional advisory committee] of which independent directors are principal members". Based on the said logic, I think it would be smoother to read, if it was written as "optional advisory committee which consists of the majority of independent directors". I'm wondering whether it was intentionally written as "primary members" or it was written in that way just as an example. If you based it on the said scenario, it would be easier for readers to understand, if written as "optional advisory

committee which consists of the majority of independent directors".

That's all.

[Ikeo, Chairman] Please go ahead.

[Callon, member] Thank you very much. I agree with many points which Mr. Ota made, so please let me follow up on some of them.

The first point is the timing of implementation. I think it is necessary to set an appropriate deadline for the appointment of multiple independent directors. We could rush the implementation, but as Mr. Ota mentioned, we should consider ensuring quality as well as transitional measures. So I think it would be more realistic to implement it in 2016 rather than the next year, and it would help companies to secure appropriate and qualified independent directors.

I also agree with the other point made by Mr. Ota, that it is necessary and appropriate to segment listed companies into groups. However, the JPX-Nikkei 400 consists of only 400 companies. To promote real reform, I would like to suggest that we should aspire to at least the TSE First Section plus Second Section. However, given that many companies in TSE Second Section are rather small in terms of market cap, the right outcome appears to be either TSE First Section or alternatively TSE First Section plus Second Section.

As for securing high-quality independent directors, I'd like to give a hats off to the Japanese people. Although the population of the UK is a half of that of our country, UK boards are required to have a majority of independent directors and UK companies secure sufficient human resources. Similarly, I believe that Japan, an economic giant, will face no problem in securing high-quality human resources for outside directors if they have sufficient time. I don't believe the country with the population of 130 million cannot secure 5,000 independent directors.

Nonetheless, Mr. Ota's points were very convincing. In order to secure high-quality human resources through a solid process, I think a certain moratorium would be necessary.

Apologies for taking up a lot of time, but may I make one more comment?

[Ikeo, Chairman] Sure.

[Callon, member] According to the independent directors of Japanese companies that I have spoken with, provided that they receive information sufficiently prior to the board meetings, they can fully participate in the discussion and fulfill their roles as directors. However, in some cases, directors are informed of the meeting agenda only on the day of the board meeting, which makes it difficult for them to participate in the discussion in any real sense. When they have to discuss pros and cons of any issue in their capacity of director, they have no ability to provide input without sufficient information. Therefore, I'd like to request that the Code clearly stipulates appropriately prior information provision to independent directors.

[Yufu, Director of the Corporate Accounting and Disclosure Division] Please take a look at Supplementary Principle 4.12.1. What Mr. Callon just mentioned is written in the codes of other countries, and a very important point from the general perspective. In Item (i) of 4.12.1, it reads "(m)aterials for board meetings are distributed sufficiently in advance of the meeting date". It means the board should ensure such information provision.

In this connection, please also refer to the box of 4.13. It states that the board should

ascertain smooth provision of such information. If the board distributes all materials on the day of the board meeting despite the fact that there is no emergency, I think the board will have to take necessary measures as specified in Principle 4.13. Besides, 4.12.1 (i) requires the board to distribute materials well in advance of the meeting. Thus, I think the intention would basically be understood without any addition or change.

[Callon, member] Understood. Thank you.

[Ikeo, Chairman] Mr. Horie will speak first, followed by other members in order.

[Horie, member] I'd like to make just one point concerning Principle 4.8. I totally disagree with Mr. Ota and Mr. Callon. I believe this should be done immediately, because we are taking 'Comply or Explain' approach. As observed upon establishing the Stewardship Code, the Japanese people tend to try to comply with every principle. That's not what it should be. According to 'Comply or Explain' principle, if companies cannot find sufficient human resources with appropriate qualifications, they should squarely explain such a fact. If we take time now, people may have a negative impression that Japan postpones dealing with a problem again. This is 'Comply or Explain'. If companies cannot secure human resources, they should properly explain the reasons. In this way, they should respond to the Code immediately, and I think this Principle should remain as it is, and companies should take a necessary action immediately.

[Ikeo, Chairman] Okay, Mr. Mori, please go ahead.

[Mori, member] Thank you. I'd like to thank the secretariat for preparing such a voluminous draft by accommodating different opinions in a short time.

As Mr. Ota and Mr. Horie mentioned, I believe that securing the effectiveness is very important. At a former meeting of the Council, we discussed that 'Comply or Explain' principle was to be stipulated in the Preamble, and thus Mr. Horie's suggestion would be one option. When keeping the Principle remained as it is, for the sake of feasibility, we should take a measure not to give individual companies a hard time, as mentioned by Mr. Ota.

Now, I'd like to briefly explain my opinion paper for today's meeting. Principle 4.11 stipulates "Preconditions for Board and Kansayaku Board Effectiveness". As written on page 2 of my paper, the principle concerning expertise of *kansayaku* includes expertise in finance and accounting, and I think it is very good to describe it in the principle. As an expected role, *Kansayaku* conducts operational audits and audits of condition of property, and thus expertise in auditing would be required of *kansayaku.* I, therefore, think it is necessary to include expertise in auditing in addition to finance and accounting.

Especially, the revised Companies Act clearly states that the right to decide on the appointment and dismissal of accounting auditors is transferred to the *kansayaku* board. Accordingly, auditing of condition of property, which leads to an evaluation of reasonableness of the accounting auditor's audit, requires the said expertise. Therefore, I believe that expertise in finance and accounting, and auditing should be required.

Thank you very much.

[Ikeo, Chairman] Mr. Uchida, please go ahead.

[Uchida, member] First, in Principle 4.7 (i), it reads "Provision of advice on business policies and business improvement based on their knowledge and experience". I'd like to request to add the wording "with the aim to promote sustainable corporate growth and increase

corporate value over the mid- to long-term". I believe these are keywords which express their important roles, so I'd like to include them here.

Next, as for Principle 4.8, I agree with other members' opinions. I'll be using different data from Mr. Ota's data. Among all 3,414 companies listed on TSE, companies which have multiple independent directors account for 13.1%, and that means the remaining 86.9% of companies need to take some actions. Considering such a situation, it is quite unlikely that all these companies will be able to comply with the principle by the general meeting next June. Individual companies will obviously make efforts for the compliance, but considering the time constraint as well as the importance of ensuring quality of independent directors, it is likely that they cannot find sufficient qualified candidates. So we need to give full consideration to a high probability of it not being feasible. Accordingly, I understand that when 'Comply or Explain' approach is described, we should explain that in case companies cannot comply with the draft principle concerning the appointment of at least 2 independent directors, they are expected to simply explain the reasons. If the Code requires the companies to state reasons why the appointment of at least 2 independent directors is not reasonable, it will create an extremely difficult situation. I understand the Code stipulates provisions in accordance with proper 'Comply or Explain' approach, so please take my point into consideration.

The opinion paper for today's meeting states that nomination advisory committee and/or compensation advisory committee should not be mentioned as an "example", but, rather, as a best practice. However, although there are some companies which actually have such optional committees at the moment, they established such committees as a voluntary initiative to increase the transparency of management. So it would be appropriate to refer to such committees as an example. In order to ensure such an institutional design as nomination committee and/or compensation committee working well, as I mentioned in the previous meeting, I think it is necessary to have an executive job market, liquidity in the labor market, and supporting education system. From the perspective of increasing the transparency, it can be achieved through the establishment and disclosure of basic policies concerning decision-making on nomination and remunerations. Concerning specific ways to increase the transparency, I believe it is essential that we leave it to individual companies' discretion and voluntary initiatives.

That's all.

[Ikeo, Chairman] Please go ahead.

[Ota, member] Let me speak for the second time.

Several members expressed opposite views to mine, and I'd like to counter-argue their points. First, Mr. Horie claimed that it should be OK under 'Comply or Explain' approach; companies could just explain if they cannot comply. I would say it is not logically reasonable. I mention this in every meeting: I'm not saying we should compromise with the reality. It is okay to give a direction to be complied with. Yet, as I showed you actual figures, most companies are unlikely to comply with the draft principle. Then is it appropriate to urge them to comply? That's what I'm saying. I'm not sure whether it is appropriate to set the transition period as one year or two years as Mr. Callon suggested, but I'm not saying we should postpone the implementation for 5 years or 10 years. But when it is realistically

infeasible for most companies, is it really desirable that most companies provide explanations? That's my point.

I also think that it is essential to consider what should be done to increase the effectiveness. I'd like to propose two measures to be taken. One is to secure human resources as I mentioned earlier, and another is to provide them with continuing education and training opportunities. Only after ensuring these two measures are in place, we will be able to make it virtually obligatory to have multiple or even 3 independent officers as discussed earlier, and companies will change accordingly. I think consideration should be made by looking at such matters.

Furthermore, concerning the expression of 4.10.1 on page 17, Mr. Oguchi mentioned that it should not be written as "committees under the board to which independent directors are primary members", but as "which consists of the majority of independent directors". However, what is meant here is not like that. Even if independent directors are not the majority, when companies are increasingly appointing independent directors, optional advisory committees should be established, headed by such independent directors. I read in this way, so I don't think it means the committees should consist of the majority of independent directors.

[Ikeo, Chairman] Ms. Nakamura.

[Nakamura, member] I have almost the same opinion as Mr. Ota. Concerning the timing of implementation of the principle pertaining to independent directors, apart from the discussion of exactly when, I think it would be better to convey a message that it is desirable to implement approximately by when, because the companies may not select exactly proper persons as independent derectors if they need to move too hastily.

In this connection – although this is applicable throughout the Code – despite the fact that we take 'Comply or Explain' approach, through the exchange of opinions with other companies I found that many companies interpret it in such a way that they have to implement what is written in the Code immediately and some are worried about that. Looking at the entire Code, including in what way companies make decisions in response and how they make announcements, the companies need a broad range of consideration. As for this Code, I think it is important for companies to undergo a process to gradually improve disclosures by conducting disclosures according to the Code, or exchanging opinions with investors. Therefore, I'd like to request that the Preamble states the importance of explanations under 'Comply or Explain'.

That's all.

[Ikeo, Chairman] Mr. Oguchi.

[Oguchi, member] I assume we will have only a couple of remaining meetings, so we should also think about how we organize the matters when we call for external opinions in December. "Easy to understand" is a keyword used in the working draft several times. Assuming that the draft proposal is to be translated into English for parties abroad, I think we should consider an easy-to-understand writing style which is received in a positive light. For instance, we earlier discussed the shortage of human resources [for independent directors] and need for time. It would be true, but smooth words make smooth ways. Impressions are different depending on whether you say "half-empty glass" or "half-full glass". So we

should emphasize the positive stance by drafting the Code in a positive manner first, and then adding provisory clauses. The content of the working draft is great, and I think what is written therein is reflecting the reality. However, I'd like to request the secretariat to find a better way of writing.

Similarly to the issue of an easy-to-understand manner, I'd like to respond to Mr. Ota's comment on my suggestion. What I mentioned earlier about 4.10.1 is a logical flow of thinking. The phrase in question starts from "for instance". So my first interpretation was like this. In case independent directors do not make up the majority [of the board], it is anticipated to establish something like an advisory committee, and such an advisory committee should consist of the majority of independent directors. I think this is a logical flow. However, as it is written as "for instance", it is understood that there are some other ways. Nonetheless, it would be easier to understand the intention if the flow was written in a straightforward manner. Thereafter, companies follow 'Comply or Explain' approach. Besides, this is written as an example. There should be other ways. Then an example should be shown in the easiest-to-understand manner. That's how I thought. I just wanted to make a supplementary comment.

[Ikeo, Chairman] Please go ahead.

[Callon, member] I'd like to make one comment on the timing of the implementation of the Code, which is that I hope that the Code will be implemented with the maximum possible speed. This Code is historic and revolutionary. The best practices of many listed companies in Japan form the basis for this Code, which will result in raising the bar for corporate governance across Japan. I'm really grateful to the fellow members of this Council. Each member has brought a different perspective from their different standpoint, but in the end all of the members have considered what is the best for the country of Japan. I think that this coming together is a great thing about Japan, perhaps even a unique strength of Japan.

I do think the Code itself should be implemented as soon as possible. However, as far as independent director requirement is concerned, I would suggest that we have a transition period of one year or so. Because Japanese companies are incredibly serious enterprises, if each company positively appoints independent directors that matches their needs based on a solid process, it will lead to a better outcome..

[Ikeo, Chairman] Please allow me to express my own opinion. As a moderator, I have been refraining from voicing my opinions, but I was asked by Professor Kanda, who is absent today, elsewhere why I had not expressed my own opinions. So let me make a comment.

It is concerning page 12, the second paragraph of the Notes. A common view of the Corporate Governance Code is that it is being established to strictly regulate the management. Unfortunately, not a few people take it as a North-Wind Policy [as in the sun and the north wind] in my observation. I will not say that there is no element like a North-Wind Policy, when we would like to see that companies will be managed in a disciplined way, with a sense of urgency. I don't think this is a North-Wind Policy. I rather feel this is a Sunshine policy. That is articulated in the second paragraph of the explanation on page 12. We are drafting the Code in order to establish the framework where the management can make bold decisions and make maximum efforts without a fear of liability for consequences. We are doing this for the sake of the management, to make it easier for the

management to exercise their skills in corporate management. I'd like everyone to understand it.

Therefore, independent directors look at the management efforts. Corporate performance does not solely rely on the management efforts. Unfortunately, there are various factors which are out of control of the management, and corporate performance also depends on the mixture of the management efforts and such factors. Accordingly, even if the management is not doing well, it is possible that the company achieves good business results. On the contrary, even if the management has made tremendous efforts, it is possible that business results are poor. If there is a fact that the management made hard efforts, even if the results are not good, independent directors should defend the management. In that sense, we are not establishing the Code as a North-Wind Policy which merely regulates the management strictly. Rather we are working for the purpose of creating a framework enabling more flexible corporate management for enhancing corporate value. I'd like everyone to understand it.

However, I'm not confident that such an intention will be understood only from the second paragraph on page 12. I would suggest that such an intention is to be written in the Preamble, so that everyone can understand that there definitely is an aspect of a Sunshine policy.

Any other comments? Mr. Takei, please.

[Takei, member] Thank you. I strongly support what Chairman just mentioned. Especially, I have also made a comment concerning the second paragraph of Notes, and I think it is about motivating the management positively for 'growth-oriented governance'. Furthermore, 4.2 refers to the support for appropriate risk-taking. I think these points should be definitely emphasized.

I have three more minor points. In response to the earlier discussion on 4.10.1, I would say that "primary members" is a good Japanese expression, and easy to understand on the contrary. Therefore, I would suggest to keep the expression "primary members" as it is. This is the first point.

The second point is concerning 4.11.2, specifically the term of office of non-executive officers. I think it is still too early to set the maximum year limit for the term. The codes of other countries take different stances toward it. I think they do not flatly stipulate that the term of office should not exceed a certain number of years. So I do not support the idea to set a limit for the term of office in 4.11.1. If we decide to stipulate it, Principle 4.11 is about disclosure of the factual situation – the number of concurrent positions of outside officers. So I don't think this is a right place. From the perspective of securing independent and outside persons in the future, I think it would be better to carefully consider the limit of the term of office. This is the second point.

The third point is concerning 4.11 qualifications of *kansayaku,* specifically knowledge in finance and accounting. I don't think we need to add "auditing" to this requirement. "Finance and accounting" is the term already used in the Companies Act. As far as I 've been searching for, none of the codes of other countries stipulate that knowledge in auditing is necessary. They do mention the term "finance and accounting", but not "auditing". If we require knowledge in auditing in addition to finance and accounting, it will become a

different story. *Kansayaku* and audit committee are expected to fulfill their duties by cooperating with internal control department and/or internal audit department, in other words, making use of individuals who have knowledge and responsibilities in auditing. So I'm not comfortable with writing "auditing" there redundantly.

These are the three points I wanted to make.

[Ikeo, Chairman] Thank you very much. Any other comments?

If you don't have any more comment on the first half, I'd like to move on to the second half. If you have any opinions or comments on the revisions and newly added principle cross-shareholdings, as well as pages 1-14 and pages 20-21, please voice them. Mr. Uchida, please go ahead.

[Uchida, member] I'd like to ask a question about Principle 1.3. It stipulates that listed companies should establish and publicize their basic strategy for capital policy. I'd like to know specifically what is expected to be disclosed. Generally, companies make fund raising decisions upon making comprehensive consideration of such factors as market environment, required fund size, reasons for financial need, and free cash flow forecast, as well as comparative study of various means. A decision on whether they go for debt finance or equity finance may be made right before the fundraising, so it is quite unlikely that companies announce their medium- to long-term basic policies. Furthermore, I have an impression that it would be difficult to announce medium- to long-term policies for purchasing treasury stocks. So I'd like to know the assumption of the Principle.

[Yufu, Director of the Corporate Accounting and Disclosure Division] It's difficult to answer the question clearly. First of all, when companies actually draft it, I can understand and I can easily imagine that they have difficulties because they cannot exclude various factors such as external environment, other requirements or influences in relation to capital policy. Taking it into account, we wrote basic strategy for capital policy, instead of capital policy itself.

[Ikeo, Chairman] It was me who asked the secretariat to include Principle 1.3. I thought the Code would seem unnatural, if it suddenly stipulated principles for particular matters such as cross-shareholdings or capital policy which may harm shareholders' interests. Therefore, I don't mean that companies should disclose specific policies showing, for instance, a certain debt/equity ratio. Rather I was thinking something like philosophy. In such a policy, they should state their basic approach to cross-shareholdings. I requested the secretariat to include it, considering that something close to business principles – I would say business principles concerning capital policy – should be included prior to the discussion of individual capital policy.

[Uchida, member] When we say capital policy, companies get an impression that they are required to write how they consider equity finance, or how they consider D/E ratio – although not a few companies have already disclosed D/E ratio – and worry about what to write. I think it will be a little difficult.

[Ikeo, Chairman] I'd like to request for reconsideration of it.

[Uchida, member] Under Principle 3.1, although this is a repetition of what I said in the last meeting, the selection of senior management and nomination of candidates for directors and *kansayaku* are made in accordance with the policy which requires to disclose as stipulated in (iv). Therefore, it is doubtful whether it is really necessary to disclose reasons for individual

selection or nomination as stipulated in (v). I know there are opinions to support it, but from the perspective of increasing earning power – which is the objective of drafting this Code, I think disclosure as per (iv) is sufficient.

Next, 4.1.3 reads "the board should approve and appropriately oversee a succession plan." Looking at this Code, companies interpret that in order to comply with this principle, they have to submit a proposal of a succession plan to the board and make a resolution. I think that procedures to make a decision on a succession plan for CEO, etc. should be left to the discretion of each company, and thus vary. Yet, this draft seems to require the procedure to obtain the board's approval. In the meantime, the meaning of "appropriately oversee" may include how to develop successors in a planned way. So I would suggest you to delete the word "approve" and state "the board should appropriately oversee a succession plan of CEO, etc."

As for Principle 5.1 concerning dialogue with shareholders, I'd like to request including the wording which clarifies that the objectives of such dialogue are sustainable growth and enhancement of medium- to long-term corporate value, as written in General Principle 5. For instance, Principle 5.1 could be revised to read "listed companies should respond to requests for dialogue (face-to-face meetings) by shareholders toward sustainable growth and enhancement of medium- to long-term corporate value". Or you could use Mr. Callon's opinion paper for the last meeting as a reference. He proposed the wording "also taking into account the number of shares held and shareholder attributes". In either way, I'd like to request that the wording is to be modified, focusing on constructive dialogue. Alternatively, although this may be extreme, it is considered to change the title of Chapter 5 to "Constructive Dialogue with Shareholders". If it is difficult, you could consider changing the sub-title of Principle 5.1 to "Policies for Constructive Dialogue with Shareholders" or "Policies for Dialogue with Shareholders Which Contribute to Sustainable Growth and Enhancement of Corporate Value".

Principle 5.2 stipulates that "medium- to long-term earnings plan" should be specified. For companies, long-term often means 10 years. In the rapidly changing environment, I have a little doubt about how meaningful a long-term earnings plan could be. As far as long-term is concerned, I think a strategy, goal or vision is more important, and showing a long-term earnings plan is not appropriate.

That's all.

[Ikeo, Chairman] Thank you very much. Please go ahead.

[Callon, member] I don't have any fundamental objection to what Mr. Uchida just stated. Yet I'm a little concerned about the view expressed on Principle 5.1. If there is a reasonable basis for the request and if shareholders want to have dialogue with companies, companies should respect this shareholder wish and have dialogue with them. For example, if company announces a dividend cut, a shareholder request to maintain the dividend may not be a medium- to long-term discussion, but if shareholders want to talk about it with the company, they should be allowed to. I recognize, of course, that constructive dialogue from the medium- to long-term viewpoint is very important, so just want to request careful and appropriate wording on this point.

[Ikeo, Chairman] Mr. Oba, please go ahead.

[Oba, member] I felt Chairman was trying to urge me to say something, so I'd like to make a comment. I understand what Mr. Ota was trying to say. To put it simply, I suppose he said that without taking the reality into account, the Code will become superficial, and thus it is a waste; so we should give a little more thought to the reality. However, considering the current situation, which is the reality, we should not forget the fact that the stock markets have made a harsh evaluation. There is a fact that we are confronted by the reality of sluggish stock prices over 30 years. Listed companies should realize it. Listed companies are public companies, and thus they exist in the public sphere. The board should consider how to address such a fact. I think such a perspective should be written in the Preamble.

As Professor Ikeo mentioned, I think it is obviously necessary to write in the Preamble that this Code is somehow like a Sunshine policy. However, this Code is also aiming at realizing a Win-Win relationship between investors and the management. In that sense, we should articulate that these Principles are anticipated to be applied to public companies as soon as possible, I think.

That's all.

[Ikeo, Chairman] Please go ahead.

[Mori, member] Thank you. I'd like to make a comment on Principle 1.2 Exercise of Shareholder Rights at General Shareholder Meetings on page 3 of the Material. We have discussed this issue at the early stage of the Council. While considering how to create an environment for shareholders to exercise their rights, I think we should keep in mind that shareholders need to properly understand the situation of the companies. As it is written in the Stewardship Code, I raised several points: what information is provided for that purpose? What about securing the period to understand, analyze and consider such information? How can we secure opportunity for shareholders to exercise their rights? Concerning the information, the most accurate information disclosed by listed companies would be securities reports. Therefore, I mentioned that securities reports are to be fully used in an effective way upon exercising their voting rights.

Concerning Supplementary Principle 1.2.1, because we are talking about listed companies, of course, disclosure documents under the Financial Instruments and Exchange Act are very important rather than disclosure documents under the Companies Act. Supplementary Principle 1.2.1 refers to "accurate information to shareholders as necessary in order to facilitate appropriate decision-making at general shareholder meetings", which I believe includes securities reports. I think this point should be clarified to a certain extent. According to my recollection, in the committee on financial system under the Financial System Council in 2009, the members argued that securities reports and internal control reports should constitute reference documents for general shareholder meetings. In the response to public comments on the draft proposal for the revised Cabinet Office Ordinance on Disclosure of Corporate Affairs, etc., the Financial Services Agency replied that securities reports and internal control reports provide important information for exercising voting rights at general shareholder meetings.

At present, only few companies issue their securities reports prior to general shareholder meetings. The vast majority of listed companies actually submit securities reports only after general shareholder meetings. The current situation does not fit in the discussion of the

Financial System Council at that time. Taking such a situation into account, I think the Code should clearly mention securities reports here.

Furthermore, concerning ensuring opportunities to exercise voting rights at general shareholder meetings – I think it is related to Supplementary Principle 1.2.3 – there is an issue of general shareholder meeting dates. We have discussed that the situation where general shareholder meeting dates are concentrated in late June may hamper shareholders' exercise of rights at general shareholder meetings, including the issue of the period for analyzing information. As convocation notices are clearly mentioned in Supplementary Principle 1.2.2, I think it would be better to clearly mention general shareholder meeting dates in Supplementary Principle 1.2.3 from the perspective of providing accurate information. For example, taking this perspective into account, it would be better to change the expression to appropriately set "the date of the general shareholder meeting and any associated dates".

That's all.

[Ikeo, Chairman] Ms. Nakamura, please.

[Nakamura, member] Concerning the point which he just made, I am not opposed to the overall direction, but considering the current situation, companies must undergo statutory audits under the Companies Act, preparation of the financial statements and annual report prior to that, as well as preparation of the earnings briefing and securities report. The administrative schedule is actually very tight. I heard that a study for streamlining such reporting is being conducted elsewhere. I'm not totally against the opinion that securities report should submit before the general shareholders meeting if, in addition to organizing and integrating those reports, the framework would be established which enables companies to set general shareholder meeting dates within 4 months – including amendment of the relevant law to address various exceptional events as written in the draft, such as the case where financial statements are not approved as a result of an audit and the company in question cannot file its tax report by the deadline. However, under the current circumstance, it is very difficult to prepare securities reports before dispatching convocation notices. I'd like to request to take it into account when finalizing the draft.

That's all.

[Ikeo, Chairman] Please go ahead.

[Mori, member] I understand the comment which Ms. Nakamura just made. Naturally, the best efforts should be made, considering various constraints such as a period necessary for preparing disclosure documents. However, it is essential to consider what information shareholders rely on to exercise their voting rights. This initiative for strengthening corporate governance, and the Stewardship Code established in February are two wheels of a cart for corporate growth. Thus, I think the intention is that each party should take necessary actions within the scope of the laws, rather than revisions of the laws.

Concerning auditing as mentioned earlier, the section titled "Ensuring Appropriate Information Disclosure and Transparency" includes principles concerning external auditor, and one of the items reads "Establish standards for the appropriate selection of external auditor candidates and properly evaluate external auditors". I'd like to repeat that duties of *kansayaku* include operational auditing and auditing of condition of property; and in terms

of expertise of *kansayaku,* I assume that it is difficult for *kansayaku* to fulfill their duties sufficiently unless they can evaluate accounting auditor's audit. This is not only a trend in Japan, but, for example, audit committees in the US are moving toward making evaluations of external auditors. In Japan, the revised Companies Act clearly stipulates that *kansayaku* or the *kansayaku* board have the right to make decisions on proposals for appointing or dismissing an accounting auditor. As a qualification required of *kansayaku,* I think such a competence is necessary and made the comment. Yet if there are some other stipulations to that effect, it may be okay.

That's all.

[Ikeo, Chairman] Now beyond the particular points of consideration, I'd like you to discuss the overall issue of the Code or what should be written in the Preamble. We do not have much time left for discussions in the future.

Mr. Uchida, please.

[Uchida, member] I'd like to make an overall comment. This is a repetition of what I mentioned in the previous meeting. The purpose of this Code is to show important principles, and thus we should allow various means and approaches for specifically how companies put Principles into practice. We need to make it widely known to users of the Code. We should avoid the situation where means are confused with principles or objectives. From that perspective, I'd like to request that the Preamble describes the following three points:

The first one is an explanation of 'principle-based'. Japanese companies are not familiar with the concept, and neither are the users. So I'd like to request that the Code clearly explains the concept. The second one is an explanation of 'Comply or Explain'. Similarly, they are not familiar with the concept, and it requires a clear explanation. The third point is to ensure that 'to Explain' will not result in an unfair negative evaluation. I'd like to request that the Code clarifies that a proper explanation should not be taken negatively.

[Ikeo, Chairman] Please go ahead.

[Oguchi, member] In addition to his view on the Preamble, as Mr. Mori mentioned earlier, the Stewardship Code, which is distributed to us as a reference material, also states that corporate responsibilities as we have been discussing and responsibilities of institutional investors as defined in the Stewardship Code are complementary by using the keyword "two wheels of a cart" in the Preamble. I assume that the secretariat is going to write about it so that the Corporate Governance Code responds to the precedent Stewardship Code. Just to make sure, I'd like to request that the Preamble describes that the Corporate Governance Code and the Stewardship Code are complementary and work together like two wheels of a cart.

That's all.

[Ikeo, Chairman] Anybody else? Please go ahead.

[Callon, member] Let me make one point that is perhaps obvious, but just in case. Unfortunately, Mr. Toyama is absent today, but he has provided an excellent written submission for today's discussion. I'd like to request the secretariat to fully consider his submission, which I totally agree with. Thank you in advance for your consideration.

[Ikeo, Chairman] Ms. Nakamura, please go ahead.

[Nakamura, member] Mr. Callon just referred to Mr. Toyama's opinion paper. I'd like to express a contrary opinion. It is about Principle 1.4 concerning cross-shareholdings on page 4. I think Mr. Toyama wrote such shareholdings should be explained to the same extent as defined in the Stewardship Code. Speaking from the corporate standpoint, our company has cross-shareholdings for the very reason of our strategies. Our company does not hold such shares from the perspective of risk vs. return on capital. Rather, we are a steward, and in a totally different position from institutional investors. Cross-shareholdings are not for the purpose of investment. Companies hold such shares from the perspective of business alliance or strengthened partnership. I do believe that it is not appropriate to treat such cross-shareholdings in the same manner as other shareholdings [for the investment purpose].

Accordingly, if such companies are required to clearly explain details of each cross-shareholding, it may lead to disclosure of details which should be kept confidential for business alliance reasons. So I'd like to request that the principle on this issue is maintained as it is now.

That's all.

[Ota, member] May I?

[Ikeo, Chairman] Sure.

[Ota, member] Mr. Callon earlier said that Mr. Toyama's opinion paper is excellent. Let me refer to two points which I'm not comfortable with. Whenever I want to counter-argue with him, he is absent. So, as usual, I'd like him to check my comments in the meeting minutes. The first point is on page 1, the second paragraph in bold font beginning with "Or, to put it the other way around". My opinion may partly overlap with Mr. Oba's opinion. As for the statement "if the Code ends up preserving the status quo", I think it was written on a specific set of values. As for the expression "preserving the status quo", I'm concerned about a risk of the Code being superficial. The real intention of my comment is how to ensure the effectiveness of the Code. I'd like Mr. Toyama to understand it.

The second point is concerning General Principle 4 on page 2. Written in bold font, it reads "even if the majority of listed companies are in fact Companies with *Kansayaku* Board" and then "it must be said that Companies with *Kansayaku* Board suffer from systemic corporate governance defects … and the fact that Companies with Three Committees (Nomination, Audit and Remuneration) are in some ways superior". I don't think so. As I mentioned before, we have discussed that the monitoring model and the management model are of equal value, so I'm very uncomfortable with picking out defects of each model or stating good and bad.

I have to repeat this. To whom do we need to explain the current situation of Companies with *Kansayaku* Board, which is the overwhelmingly dominant institutional design? To those who do not know it. I always point out the necessity of such an explanation.

Furthermore, although he states Companies with *Kansayaku* Board, which adopt the management model, are weak in terms of the evaluation of the management by outside officers, but that is nothing but a very difference between the management model and the monitoring model. Only because of that point, we should not discuss good or bad. In conclusion, regardless of which model a company adopts, each company is required to not merely to comply with laws and regulations, but to take creative measures which suit its own

situation or provide necessary explanations. This is the fact, and we should just emphasize this point.

That's all.

[Ikeo, Chairman] Please go ahead.

[Uchida, member] Concerning shareholdings for policy reasons, at the last meeting, I thought Mr. Toyama agreed with my view, but it is not necessarily true, judging from his opinion paper. I may oppose Mr. Callon's opinion. Requiring companies to disclose returns and risks of each shareholding, as shareholdings for policy reasons are linked with individual projects, will result in requiring disclosure of profitability or return from individual projects, thus being strategically difficult. The current proposal states that the board should examine such aspects of shareholdings for policy reasons, and I think the Code should maintain the current stipulation. The exercise of voting rights is also linked with strategies, so it is also difficult to disclose. Therefore, I disagree with Mr. Toyama's opinion.

[Ikeo, Chairman] Please go ahead.

[Callon, member] I feel like I opened Pandora's Box! To restate my point, I think it is a very good submission. Specifically, I totally agree with his view on cross-shareholdings. I think the draft wording of the Code concerning cross-shareholdings is insufficient, but I can appreciate the progress toward enhanced disclosure. I'm sorry to have to put it so directly, but as long as you are a listed company, you are accountable for the exercise of their voting rights of their cross-shareholdings. It is wrong to believe that just because you are a "listed company" holding shares "for strategic reasons", the Stewardship Code does not apply to you. Nonetheless, I do support the Code's draft wording which at least progress.

[Ikeo, Chairman] Are there any other comments? If you do not have any additional comments, I'd like to close the discussion.

As I mentioned earlier, by the next Council, the secretariat will prepare the complete working draft for the proposal of the Code, including the Preamble, based on the discussions of today and previous meetings. Next time, we will discuss the finalization of the draft proposal.

Thank you very much for your active discussion and many inputs. As usual, if you have any additional comments or requests, please send them by e-mail or other means. If you remember something you forgot to mention, please write to the secretariat.

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

[Yufu, Director of the Corporate Accounting and Disclosure Division] The next Council of Expert is tentatively scheduled to begin at 16:30 on Friday, December 12, although the secretariat is still coordinating the schedule. We will inform you of the details later. Thank you in advance for your cooperation.

[Ikeo, Chairman] Thank you very much.

Now I declare today's Council closed. Thank you very much for your cooperation.

End