

**The Twenty-First Council of Experts Concerning the Follow-up of
Japan's Stewardship Code and Japan's Corporate Governance Code**

1. Date and Time: November 18, 2020 (Wednesday) 16:00-18:00
2. Venue: 9F, Central Government Building No. 7, Meeting Room

[Kanda, Chair] It's already the scheduled opening time, so I'd like to open today's meeting of the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code. This is the twenty-first meeting. Thank you very much for taking the time from your busy schedule and participate in this online meeting,

Today, as explanations from the Secretariat, a representative from the Financial Services Agency (FSA) will provide an overview of the points raised during the past meeting as issues on "corporate governance in the economic and social environment after COVID-19". Then, a representative from the Tokyo Stock Exchange (TSE) will explain the current discussion on corporate governance in connection with the review of the market segments. Then the FSA representative will explain governance required for companies to be listed on the Prime Market, as well as the issues to be discussed concerning board effectiveness. After all explanations are given, I'd like to ask the members to initiate a discussion.

We will proceed with today's meeting in that way. Today, Ms. Waring will express her opinion in English, and there will be consecutive interpretations.

Now, I'd like to ask the FSA to explain the points raised during the past meeting as issues on "corporate governance in the economic and social environment after COVID-19".

I'm handing it over to you, Director Shimazaki.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] I'll explain it according to Material 1 "Discussion at the 20th Council (Summary)".

In the previous meeting, we presented a range of subjects, both general and specific, and you expressed various opinions on them. Thank you for your inputs.

From page 1, we sorted out your opinions into certain categories: general remarks, and specific comments on the issues we raised at that time, namely, the board, awareness of cost of capital,

sustainability, ensuring confidence in audits, and group governance.

Starting from general remarks, for example, about corporate governance after COVID-19, need for accelerated response to changes, and digital transformation, we received various opinions, although I won't explain the details now. Thank you very much. The opinions are listed up to page 13.

On page 14, we summarized the subjects to be discussed today and going forward, according to your discussion on challenges, general issues, and points to be discussed. Specifically, the subjects include the board effectiveness, business management with awareness of cost of capital, ensuring confidence in audits – these are what we presented in the previous meeting – as well as general shareholders' meetings, and mid- to long-term sustainability. Furthermore, as issues towards corporate reforms after COVID-19, it was suggested that the Council should discuss DX, human resources, and risk management that corresponds to the increased uncertainty, although there may be overlaps with the above-mentioned issues. We suggest that the Council should focus on the topics listed herein as the issues of corporate governance for corporate reform after COVID-19, although the focus is not necessarily limited to them. That's what Material 1 is about.

[Kanda, Chair] Thank you very much.

Next, I'd like to ask the representatives from the TSE and the FSA to explain the current discussion on corporate governance in connection with the review of the market segments, and points to be discussed concerning governance required for companies to be listed on the so-called Prime Market. I'll hand it over to you.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] First, the TSE will introduce Material 2 "Discussion on Corporate Governance for Review of TSE Cash Equity Market Structure", and then the FSA will provide an explanation by using Material 3 "Required Corporate Governance for Companies Listed on the 'Prime Market'".

Could you please start?

[Ao, Executive Officer, TSE] I'm Ao from Tokyo Stock Exchange. Let me share the current situation regarding the review of the market segments and the related discussion about the corporate governance at each of the market segment.

The progress is summarized on page 3 of Material 2. With respect to the review of the market segments, at the end of 2019, the Expert Study Group on Capital Markets under the Financial System

Council published a report, upon discussion with a wide range of listed companies, market participants and stakeholders. In response to the report, TSE published the “Overview of Market Structure Review and Outline of the New Market Segments” in February 2020, and is currently in the process of finalizing the details.

The overview of the review is shown on Page 4. Its objective is to help listed companies achieve sustainable growth and increase mid- to long-term corporate value. While there currently are five market segments, it is planned to reorganize the market into three segments: Prime Market, Standard Market, and Growth Market. In doing so, based on the concept of each new market segment, the scope of application of the Corporate Governance Code will be reviewed as well.

From page 5, it shows the concept of each market and the overview of the listing criteria proposed by the Expert Study Group on Capital Markets. First, the concept of the Prime Market is defined as a market for companies that have a high quality of corporate governance, and focus on constructive dialogue with investors. Accordingly, as stated at the middle of the Material, companies to be listed on the Prime Market will be required to pursue a higher standard of corporate governance continuously as the Code, etc., gets revised. And we’d like you to take this point into account during the discussion at the Council.

Page 6 is about the Standard Market and the Growth Market. In case of companies that select the Standard Market, they are not required to pursue a higher standard as in the Prime Market. As stated in the middle of the Material, however, the companies are expected to have basic corporate governance standards. Currently, the companies listed on TSE Second Section are subject to all Principles of the Code, while the companies listed on JASDAQ Standard Market are only subject to General Principles. Since it is not appropriate to lower the current level of corporate governance requirements, it is all Principles of the Corporate Governance Code would be applied to companies to be listed on the Standard Market. As for the Growth Market, considering that the market is intended for emerging companies with high growth potential, applying only General Principles would be appropriate, as is the case for those companies currently listed on MOTHERS market.

Page 7 shows the schedule of the transition to the new market segments. Details of listing criteria will be announced within this year, and the Corporate Governance Code is expected to be revised next spring or later, based on the discussions at the Council. Taking into account the criteria and the revised Code, each of the existing listed companies will select a new market segment, starting from

September 2021. The transition itself is scheduled in April 2022.

Next, I'd like to share the discussion at the Expert Study Group on Capital Markets concerning governance expected for the Prime Market.

Page 9 and onward covers such topics as the board independence as well as the establishment and independence of advisory committees. With respect to the number of independent directors on board, it was pointed out that it should be at least one-third or the majority of the board, taking overseas practices into account. The Study Group also offered the view that the companies should establish Nomination Committee and Remuneration Committee, and verify the effectiveness of each committee.

From page 10, you can see the data concerning the board and Nomination Committee or Remuneration Committee of the companies listed on the First Section. As shown in the upper-right graph, little less than 60% of the companies appointed at least one-third of directors as independent directors. In the meantime, as shown in the lower-left graph, only a small number of companies appointed the majority of directors as independent directors.

Page 11 shows whether companies have Nomination Committee and Remuneration Committee. Approx. 60% of the companies listed on the First Section have established either of such committee.

Page 12 is about independence of such committees. At more than 60% of the listed companies, each of the two committees is composed of by a majority of independent directors. Additionally, at majority of the companies, such a committee is chaired by an independent director.

And, the section starting from page 13 is about constructive dialogue with investors, which is another key requirement of the Prime Market.

On page 14, we have quoted parts of the discussions at the Expert Study Group on Capital Markets. It was pointed out that, in order to facilitate constructive dialogue with investors, it is important for companies to disclose information, which will be the basis for the dialogue, and have opportunities to communicate with investors.

Page 15 listed up agenda items, on which the Guidelines for Investor and Company Engagement and the Corporate Governance Code require clear explanations. We consider it is also important for the listed companies to actually disclose information on these items.

Page 16 provides, as a reference, actual examples of some companies' disclosure materials.

Page 17 is about disclosure in English. Many investors are not satisfied with the current

disclosure practices of the listed companies. Of course, it is not like every single document needs to be translated into English, so we believe that it is necessary for the listed companies to enhance their disclosures in English, taking into account both investors' needs and burden on the companies.

The last section seeks ways to ensure governance required for companies listed on the Prime Market.

Please take a look at the second box on page 19 of the Material, Discussions (excerpts). Many members of the Expert Study Group on Capital Markets argued that 'Comply or Explain' approach should be maintained in light of the spirit of the Corporate Governance Code. If there are any requirements which must be complied with, they should be defined as mandatory requirements elsewhere, for example, in the listing criteria, but not in the Code.

The current listing criteria which is in the Securities Listing Regulations, stipulates the minimum mandatory requirements that must be complied with: for example, the exercise of voting rights in writing, and the appointment of independent directors.

From page 21, corporate governance codes in other countries are shown for your reference.

Page 21 shows a comparative table of the codes in other countries.

Page 22 is about the UK's code. Some provisions contain different requirements by company size.

I'm sorry for my rough explanation. That's all from me. Thank you.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] Today we'd like you to discuss the board effectiveness and other matters, which I will explain later. Before the discussion, on behalf of the FSA, I'd like to explain Material 3 "Required Governance Required for Companies Listed on the 'Prime Market'", which consist of only one page. As just explained by the TSE, while we are going to require the companies to be listed on the Prime Market to ensure a higher level of corporate governance, there remain some matters to be considered. Specifically, we need to consider whether we should continue to adopt 'Comply or Explain' approach, or force the companies to comply with the requirements, or go for the mix of these two. Another point is rather technical: whether we should describe different expectations in a single Code. Furthermore, when we say a higher level of corporate governance, we need to consider specifically what kind of matters should be required, and what viewpoint we should take. In the bottom-right box, we listed up examples of such matters: the number of independent directors on the board, independence of advisory

committees, and so forth, as explained earlier.

That's all for the explanation of Material 3.

[Kanda, Chair] Thank you very much.

Now I'd like to ask the FSA representative to explain points to be discussed concerning the board effectiveness.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] Now I'll explain Material 4 "Board Effectiveness and Ensuring Diversity". From page 1 to page 3, we summarized the recent move of the Government.

The Prime Minister stated in his Policy Speech, "Corporate governance reform is key in raising the value of Japanese companies. To spur further growth, we will promote appointments of women, non-Japanese and mid-career professionals, and advance reforms with a view to realizing workplaces with diversity and business management free of shackles."

Page 2 is an excerpt from a joint opinion statement submitted by experts for the Council on Economic and Fiscal Policy. The experts referred to "further promoting outside directors, increasing the mobility of management personnel through significant promotion to executive candidates for women, mid-career recruits, foreign nationals, young people, etc., and securing diversity", as well as the revision of the Corporate Governance Code.

Page 3 shows excerpts from other opinion statements from the experts, namely, Mr. Niinami, Mr. Yanagawa, and Mr. Takemori, concerning independent directors and human resource development.

The next section is related to the subjects, which we'd like you to discuss, as written on pages 18 and 19. In order for companies to make prompt and decisive decisions while recognizing the challenges and getting ahead of the changes after COVID-19, we need to discuss the board composition in terms of an appropriate mix of knowledge, experience, and abilities. On page 4, we quoted our research results concerning the attributes of independent directors of JPX-Nikkei 400 companies. With respect to the combination of knowledge, ability, and experience, in case companies have 2 independent directors, approx. 70% of boards include independent directors from other companies. In case companies have 3 or more independent directors, the ratio is even higher. With respect to specific background of those from other companies, approx. 80% or 91% of boards include those with experience as president, chairman, and representative of other companies.

Please turn to page 5. With respect to the combination of knowledge, abilities, and experience

required for directors, it was pointed out that it is important for companies to consider the skills necessary for their own directors in light of their business strategies, and to realize an appropriate combination of knowledge, experience, and abilities through the appointment. At the bottom, we included some examples of companies that use a skill matrix.

I'm moving on to page 6. We cited provisions of corporate governance codes of other countries, which refer to a combination of expertise. For example, the UK's code stipulates that the board should have a combination of skills, experience, and knowledge. The UK's Guidance refers to the use of skill matrices as well. Furthermore, Germany's code and ICGN's Principles also refer to the so-called skill matrix.

Please turn to page 7. What I just explained is to some extent related to the quality of the board, but this page is about the quantity. As the TSE also explained earlier, among the companies listed on the TSE First Section, approx. 95% of them appointed at least 2 independent directors; approx. 60% of them appointed at least one-third of independent directors on the board; and 6% of them have boards with the majority being independent directors. You can see such data here.

I'm moving on to page 8. This reference material shows how governance codes or listing rules in other countries stipulate the number of independent directors on board. In many countries, it is stipulated that the majority of the board members should be independent directors. Some countries require at least one-third of board members as independent directors.

On page 9, you can see that an increasing number of companies have established a statutory or optional Nomination Committee and Remuneration Committee. Currently, which currently account for around 60% of all companies listed on the TSE First Section.

Page 10. As for optional Nomination Committees and optional Remuneration Committees, on average, the majority of committee members are independent directors. However, in a considerable number of companies, independent directors do not account for the majority of committee members.

Page 11 shows provisions of corporate governance codes concerning Nomination Committee and Remuneration Committee in other countries. As for a Nomination Committee, the UK's code stipulates that a majority of the committee should be independent directors. In Germany, it is stipulated that the committee should be composed exclusively of shareholders. In France, it is provided that the committee must mostly consist of independent directors. Similarly, we summarized provisions concerning Remuneration Committees in the UK, Germany, and France.

Page 12 is about CEO succession plan. Companies that supervise CEO succession planning account for only approx. 30%, and approx. 80% of such companies use a Nomination Committee.

Please turn to page 13. With respect to both appointment and dismissal criteria of CEOs, approx. 40% of the companies responded that they have already reviewed and revised the process, whereas approx. 30% of the companies answered either they don't have a clear idea of when to start discussion toward the revision, or they don't know.

The next topic is about diversity. The data on page 14 shows that women account for 6.2% of all directors and officers of listed companies, and the data on page 15 shows that women account for 15% of all managerial positions.

Page 16 shows the data related to mid-career hires: the larger the number of employees in a company, the lower the mid-career higher rate.

Page 17 is about human resource investment. While 56.1% of investors place importance on human resource investment, only less than 40% of companies do so. Furthermore, three quarters of the companies have not at all or not really been able to hire, deploy or train the human resources necessary for realizing their business strategies.

Finally, I'd like to explain pages 18 and 19 – subjects which we'd like you to discuss today. Page 18 is about board effectiveness, mainly focusing on the board composition. What should the composition of the board be like, in order for companies to be able to make prompt and decisive decisions while recognizing the challenges and getting ahead of the changes after COVID-19? To lead corporate reforms after COVID-19, it is considered more important for boards to be well-balanced in knowledge, experience, and abilities. What do you think about board composition, including the improvement of the quality of independent directors, for example, through the appointment of management executives with diverse management experience? And, while the majority of the companies listed on the TSE First Section have appointed at least one third of board members as independent directors, and such a practice is becoming more common in Japan, many other countries require boards to have a majority of independent directors. Given this situation, how further enhancing the number of independent directors should be considered? Furthermore, while the appointment and dismissal of the CEO as well as the candidate selection process are the most important strategic decisions, how should we consider these matters for enhancing board effectiveness? For example, one possible option would be enhancing the roles and functions of the

Nomination Committee, by making independent directors a majority of members. We'd like you to discuss these points.

Page 19 is about diversity. Similarly, how should we consider diversity in a company in order to enable companies to make prompt and decisive decisions, while recognizing the challenges and getting ahead of the changes after COVID-19? As shown in the current Code, the existence of diverse perspectives and values reflecting different experiences, abilities, and attributes within a company can be a strength. To lead corporate reforms after COVID-19, what should be considered with respect to ensuring diversity in gender, international experience, professional backgrounds, etc. in directors as well as those in managerial positions who are director candidates and core human resources? In particular, with respect to the appointment of women, foreigners, and mid-career hires in managerial positions, as well as the recruitment of human resources important to ensure diversity, what do you think about requiring companies to set voluntary and measurable targets, and disclose such targets and achievements? Furthermore, it has been pointed out that in order to ensure diversity within an entire company, it is important to develop human resources and improve the internal environment, including diverse work styles and career development. We'd like you to express your opinions on this point.

I briefly covered all the topics. That's all from me.

[Kanda, Chair] Thank you very much.

We received opinion statements from Ms. Okina and Mr. Toyama, who are absent today, so I'd like the Secretariat to share the summary of their statements.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] First, I'd like to share opinions from Ms. Okina. She pointed out that the board composition should reflect an appropriate mix of appropriate experience, abilities and knowledge. Instead of merely formal disclosure, it is important to be able to provide investors with explanations on a portfolio of independent directors that suits the company's strategy. In addition, she referred to a variation in years of service as director, as well as the Nomination Committee's involvement in the process of appointing independent directors.

Similarly, as for the appointment or dismissal of the CEO and the candidate selection process, it is vital that the Nomination Committee, which comprises a majority of independent directors, fulfills its function. The Remuneration Committee should also comprise a majority of independent directors.

And it is important that both committees should regularly report on their activities to the board.

With respect to sustainability, she commented that the board needs to discuss the matter, for example, by establishing a sustainability committee, and to oversee the business execution.

She pointed out the importance of disclosing the efforts to ensure diversity of inside directors and managerial positions, and presented some examples: the ratios of full-time female, foreign, and mid-career employees by age, as well as human resources development programs and working practices. She also argued that investors are expected to engage with companies and discuss the development of diverse human resources.

Next, I'll share Mr. Toyama's opinions with you. He expressed his view that the real reason why Japanese companies underperform their Western counterparts in terms of ability to invest for the future is the insufficient earnings power of their core businesses. Therefore, the starting point is the establishment of strong management leadership, and a strong board of directors should appoint a strong management team and endorse strong leadership. From this point of view, he explained matters to be included in the Code.

The Nomination Committee should include independent directors with a range of management experience, and companies in the Prime Market should have the committee comprising a majority of independent directors. With respect to diversity, the board should incorporate different aspects of diversity, including professional background (experience in management or professional executive roles, such as CFO), nationality and age, as well as gender. Furthermore, companies in the Prime Market should in principle have a majority of independent directors on their Nomination Committee.

As for the pool of candidates for the management team as well, diversity should apply not only to gender, nationality, and career path, but also to whether to hire graduates or mid-career employees (including rehiring former employees). He suggested that an effective way of promoting the diversity of such candidate pools over the long term should be to set optional numerical targets for women, foreigners, and mid-career hires to management level appointments. Moreover, to address the asymmetry of information that occurs with outside directors, he expects inside directors to participate in the board from the viewpoint of the entire company, and expressed his opinion about diversity of inside directors, emphasizing the importance of mid-career hires with work experience in other companies.

That's all.

[Kanda, Chair] Thank you very much.

Taking these explanations into account, I'd like you to ask questions or express opinions. As explained by the Secretariat, there are certain points to be discussed today. Specifically, such points are written on pages 18 and 19 of Material 4. I'd appreciate it, if you would focus on these points.

As usual, if you would like to speak, please use the chat function, and send a message to all participants.

Today, I heard that Ms. Waring will speak first. Ms. Waring, where are you now? Are you in the UK? I'm handing it over to you.

[Waring, member] Hello Chair Kanda and Fellow Council members. Thank you for the opportunity to present ICGN opinion on board effectiveness. My comments will focus on board leadership, diversity, independence, and appointments.

First, in terms of leadership, ICGN recommends that there should be a clear division of responsibilities between the role of the chair and the chief executive to avoid unfettered powers of decision-making in any one individual. The two roles are very distinct, and we should not expect the CEO to be "marking his own homework". The board chair should be independent on date of appointment. We discourage the practice of a company's retiring CEO remaining on the board as a director or becoming chair, regardless of any interim break period.

I would add that it is also now common practice for the chair to hold regular meetings with other independent directors without the CEO present.

As we've discussed, boards should establish a Nomination Committee, led by an independent chair and comprised of a majority of independent directors, to manage the process for the recruitment, dismissal, and adequate succession planning for the CEO.

We encourage that more companies in Japan appoint a lead independent director, even if the board chair is independent. This person can act as a point of contact if there is any contentious issue(s) arising around the role of the chair or significant shareholders.

We encourage companies to promptly respond to requests for constructive engagement from investors, whether individually or collectively. And we should be open for all dialogue on matters of material relevance to a company's strategic direction, governance, risk management, and performance.

Next, in terms of board diversity, ICGN recommends that boards should disclose both a board

policy and a wider company policy, to encompass managerial positions on diversity. This policy should include specific goals, measurable targets, and a time period over which it is achieved.

An annual report on diversity should include an explanation for the rationale for the policy, progress achieved, and how diversity is considered as part of succession planning on the board and throughout the company.

ICGN does not take a position on the optimal level of female representation on boards but we do observe that a minimum threshold of 30 to 33% is a helpful starting point.

We also recognize that the concept of diversity goes beyond gender and encompasses a range of factors, including different nationalities, professional backgrounds, social and economic origins, and personal attributes.

In terms of independence, I concur with Toyama-san. Corporate boards should have a majority of independent directors. For listed subsidiaries there should be a majority of independent directors to mitigate infringements to minority shareholder interests.

We also think it would be helpful to have a clear definition of what independence means, described in the Japan's Corporate Governance Code, because this would provide further clarity to boards in terms of their independent director appointment processes, strengthen criteria, and lead to greater consistency of approach.

My final point is about board appointments. The Nomination Committee should lead the process for the appointment, evaluation, and succession planning for independent directors, based on objective criteria. The rationale for each individual director appointment should be publicly disclosed, including any factors that might impede their independence and how the director's experience is aligned with the company's long-term strategic needs, diversity policy, and succession planning.

To ensure periodic refreshment of the Board, ICGN recommends that companies disclose specific term limits for director tenure. A director's annual re-election should be contingent on individual performance based on satisfactory evaluations of the director's contribution to the board.

Companies should also undertake a rigorous review of the performance of the board as a whole, the performance of the committees, the chair of the board himself should be appraised by the Lead Independent Director and Nomination Committee.

And finally, it is good practice for the board to be periodically evaluated by an external consultant. This review of performance would allow for long-standing directors to step down and unlock

vacancies to enable appropriate refreshment, diversity, and independence.

Thank you for your consideration.

[Kanda, Chair] Thank you very much, Ms. Waring. I'm sorry that the audio quality was not always good. We will make up for the poor audibility by preparing meeting minutes later.

Now I'd like to hear questions and opinions from other members. As I mentioned earlier, if you would like to speak, please use the chat function and send your message to all participants.

Mr. Tanaka, please go ahead.

[Tanaka, member] Thank you. In response to Ms. Waring's speech, I'd like to make a comment, as I'm concurrently assuming the roles of Chairman of the Board and President & CEO.

In Material 1, with respect to the purposes of the current corporate governance discussions, "acceleration of responses to changes" is written in the summary of our discussions at the previous meeting. I remember the remark made by Mr. Kawamura, a former member of this Council. When he became President of Hitachi, Ltd., he considered that it would be better to concurrently assume the roles of Chairman and President to drive changes, so he first became Chairman & President. He mentioned that holding both positions enables the acceleration of a transformation. I totally agree with him.

For example, setting board meeting agendas is very important. Indeed, if an independent director chairs a board, agenda items will be very different. In case President & CEO chairs a board like in my case, while various projects are underway, the chairperson can determine an appropriate timing to report to the board or to request a board resolution in accordance with the actual progress of project execution. In contrast, in case an independent director chairs a board, the chairperson cannot make such judgments, and as a result, board meetings tend to become merely formal. Moreover, in case the positions of Chairperson and President are held by separate persons, it may give rise to a conflict, and result in a management disruption. Especially, since there are very few professional independent directors, I'm afraid such cases are likely to happen.

I understand Ms. Waring's point, but "Chairman & CEO" is very common in companies in the east coast of the USA, and I believe that it is not always necessary to get rid of such dual roles at this stage. However, there is a premise: "check and balance" is required. It is necessary to check Chairman & CEO to prevent his/her self-righteous way of managing the company.

In this regard, for example, our company has 9 directors, and two-thirds of them are independent

directors. I – Chairman, President & CEO – am not a member of Nomination Committee and Remuneration Committee. We have a lead independent director, who organizes meetings only for independent directors. In short, instead of going along with every single suggestion in Mr. Waring's paper, it would be appropriate that each company adopts a combination of suggestions that best suit the company.

Now I'd like to make some comments concerning today's topics on pages 18 to 19 of Material 4. It refers to the appointment of management executives with diverse management experience, in order to improve the quality of independent directors. We have also considered this point seriously. In reality, it is extremely difficult for non-practitioners to understand corporate management. And it takes considerable time to educate such people. Therefore, we think it is desirable to appoint practitioners who have worked for multiple companies, preferably with experience of failure. I believe that independent directors necessary for companies are not those who merely satisfy formal criteria, but those who have such substantive experience.

The most problematic case would be those who serve as independent directors as a way to make a living. My colleague, who has served as a board member in the US, repeatedly emphasized this point. In case of such people, there seems to be a conflict with the position of independent director. They are sensitive to feelings of President or Chairman in order to retain their positions as directors – not to be dismissed. So there is an incentive that they should surmise intentions of President or Chairman and act accordingly. Therefore, my colleague argued that we should exclude such people who seek the independent director's position to make a living.

Next, it is written that the companies listed on the TSE First Section have appointed at least one third of independent directors, and so forth. I have referred to Principle 4.3 of the Corporate Governance Code several times in the past. As the roles of the board, Principle 4.3 of the Corporate Governance Code stipulates: "the board should effectively oversee the management and directors from an independent and objective standpoint." With respect to the independence and objectivity, the fact that one-third of board members are independent directors means that the remaining two-thirds are inside directors. I've been wondering whether the board can play the supervisory role independently and objectively, when two-thirds are inside members. In other words, two-thirds of board members comprise Chairman, President, and their subordinates. The idea of the Corporate Governance Code is that the board itself should maintain its independence and objectivity.

Specifically, I believe that the majority of board members need to be independent directors, at least in case of companies in the Prime Market. Based on this belief, our company appointed two-thirds of board members as independent directors.

As I mentioned earlier, the next part of the Material refers to the composition of committees with the majority of independent directors. As for Nomination Committee, some people understand that, if a director serves as a member of Nomination Committee, such a director will not be dismissed. Nomination Committee members have a sort of authority over personnel matters. In that sense, it would be necessary to define a tenure in order to refresh the members. I hear that rotation of committee members is a common practice in Europe and the US. Besides, CEO and Chairman should not be members of Nomination Committee, as they must be aware that their continuation or dismissal is up to Nomination Committee. Accordingly, although Material 4 suggests that the majority of the committee members should be independent directors, I believe that basically CEO should not participate in Nomination Committee unless it is necessary to do so, and Nomination Committee itself should consist only of independent directors.

Finally, I'd like to talk about diversity on the next page. This is very simple. It depends on the CEO. As for the issues of diversity, women's participation, or appointments of diverse human resources, if CEO or President is determined to take action, much will be done. In our company, while I took the chair of President in January this year, there was no female director in the past. Now we already have one female director. We also have one female executive officer for the first time in the company's history, and two female corporate officers, in contrast no women last year. We also have women at the division manager level, in contrast to no women last year. Basically, if CEO is determined, the company can start from scratch and make achievements in many ways.

However, as for approaches for doing that, realistically speaking, promotion from within a company takes a long time, especially in Japan in relative terms. From my experience, the easiest way to address the gender issue and consider diversity would be the use of mid-career hires.

That's all.

[Kanda, Chair] Thank you very much, Mr. Tanaka.

I received many chat messages from the members. According to the order of messages received, Mr. Obata, Mr. Tsukuda, and Mr. Kansaku will speak respectively. Mr. Obata, please go ahead.

[Obata, member] I'm Obata. Thank you for the opportunity to speak. I'd like to make a few

comments including some on board diversity.

I fully agree that it is necessary to ensure diversity of the board and corporate executives under the board in a way to include women, foreigners, and mid-career hires. Especially, in this era of uncertainty, I believe it is essential.

I got an impression that this topic is selected for today's discussion in connection with the new market segments of the TSE. I suggest that we should sort out how we classify companies, particularly the relationship between organizational structures under the Companies Act, such as Company with Three Committees (Nomination, Audit and Remuneration), and Company with *Kansayaku* Board (i.e. Company with Audit & Supervisory Board), and such new market segments as Prime, Standard and Growth. If there is any confusion or conflict in this aspect, I'm afraid that the revised Code may become confusing. This is my first point.

My second point is whether a board of a company is oriented in the direction of an Advisory Board or the so-called Monitoring Board. For example, our board is still more like the Advisory Board. Depending on such an orientation, necessary attributes of directors, particularly independent directors, may differ, even in Companies with *Kansayaku* Board. In case boards are more like the Advisory Board, those with experience as President or Chairman of other companies would be effective. In contrast, in case of the Monitoring Board-type, we would see increased effectiveness of such experts as lawyers and accountants. So I suggest that we should consider how we should organize this issue.

Finally, I feel that companies are not yet clear about what they expect from independent directors. Currently, companies provide certain information as reasons for appointing independent director candidates in their convocation notices for shareholders meetings, but I assume companies have not yet clearly defined their expectations for directors, independent directors. I'd appreciate it, if the Council discussed this point – how the companies should address this issue – as well.

That's all from me. Thank you.

[Kanda, Chair] Thank you very much.

Next, Mr. Tsukuda, please go ahead.

[Tsukuda, member] This is Tsukuda. Thank you for the opportunity to share my views. I'd like to make some comments on today's topics.

First, on page 18 of Material 4, it first mentions that companies "make prompt and decisive

decisions, while getting ahead of the changes”, and I understand this is the most important. The authority is concentrated in the CEO, and the board shifts its focus to the oversight: in other words, the board becomes more like the Monitoring Board, and deliberations at the board focus on such essential agendas as the development of the mid- to long-term growth strategy, the supervision of business execution, or restructuring the business portfolio, including a withdrawal from a business, and boldly leave business execution to the CEO. I consider this is the major premise of making prompt and decisive decisions. Accordingly, as for the board composition, as long as a board is becoming more like Monitoring Board, for example, when the Prime Market requires a higher level of governance, a majority of board members should be independent directors; and in case of companies in other market segments, at least one third of board members should be independent directors. I believe that’s what they should be.

My next comment is about Nomination Committee. In the first place, roles expected for Nomination Committee are the supervision of the incumbent CEO’s execution of duties, and the appointment/dismissal based on the result of the supervision, as well as succession planning. Therefore, the most important thing is that independent Nomination Committee, regardless of whether it is statutory or optional, secures independent directors who have qualifications to play the expected roles. In that sense, I believe that it is ideal to appoint Committee members who have, for example, insightfulness, ability to listen to others and ask questions, humbleness, and courage.

In terms of the composition of Nomination Committee, as Mr. Tanaka mentioned earlier, there is an issue whether the incumbent CEO could be a member of Nomination Committee. In the large majority of Japanese companies, incumbent CEOs used to be the members of their Nomination Committees. However, in the past couple of years, an increasing number of Nomination Committees have not included incumbent CEOs, because the Committees are in a position to evaluate the incumbent CEOs’ execution of duties. Whether or not an incumbent CEO becomes a Nomination Committee member depends on individual circumstances of each company, but in any case, I believe that companies need to consider the composition of Nomination Committee members upon realizing anew the expected roles of Nomination Committee.

My final point is about ensuring diversity. I’d like to share an episode of a president of a company listed on the TSE First Section. The president was enthusiastic about assigning women to managerial positions, and strongly committed to women’s participation in the workplace. And it started to yield

positive results. Nonetheless, just because there was no female board member, proxy advisors issued recommendations to vote against the president. As a result, the number of votes for the president was much smaller than those for other directors. In the meantime, looking at other companies, there are cases where they appointed one female independent director, but their presidents are not keen on women's participation. Under such circumstances, when we discuss diversity, we should consider whether ensuring diversity is an end or a means, and whether ensuring diversity leads directly to an increase in corporate value in the first place. I believe we should re-explore this issue from such a perspective. Realistically, the revised Code could promote women's participation by encouraging companies to voluntarily disclose certain indicators, for example, the ratio of women in managerial positions. I would appreciate it, if you considered such a mechanism to encourage long-term sustainable efforts of the companies.

That's all from me.

[Kanda, Chair] Thank you very much.

Next, Professor Kansaku, please go ahead.

[Kansaku, member] I'm Kansaku. Thank you.

I'd like to make three points. Let me give you the premise first. As reported in today's Material, the number of independent directors has significantly increased since the introduction of the Corporate Governance Code in 2015. Nearly 60% of companies have already appointed at least one-third of board members as independent directors, and three-fourth of JPX-Nikkei 400 companies have done so. Furthermore, an increasing number of companies have utilized an optional Remuneration Committee and an optional Nomination Committee. According to the earlier report, Nomination Committees have been established in a little less than 60% of companies, and Remuneration Committees have been established in more than 60% of companies. At least formally, we see the progress in the appointment of independent directors, as well as the establishment of optional Nomination and Remuneration Committees. Given such a premise, I'd like to make three points, mainly targeting companies to be listed on the Prime Market, from the perspective of effective monitoring of the management, which is one of the roles and responsibilities of independent directors as stipulated in the second item of Principle 4.7 of the Corporate Governance Code.

First, although I don't have sufficient insights for suggesting an appropriate percentage of independent directors, I think the Code could set at least a target ratio of outside directors, and if

possible, require companies to set certain targets with regard to how they ensure diversity, disclose such targets, and periodically review them. This is my first point.

My second point is about optional committees. The current Corporate Governance Code stipulates both optional Nomination Committee and optional Remuneration Committee in Principle 4.10 and Supplementary Principle 4.10.1. However, I understand that functions and roles of these two committees are very different, so I'd like to suggest that the Code should describe Remuneration Committee and Nomination Committee in separate principles for further elaboration. Especially, with regard to Remuneration Committee, due to the revision of the Companies Act in 2019, after decisions on directors' remuneration are delegated by a general shareholder' meeting to the board, if decisions are sub-delegated to another body, the company in question will be required to disclose information about the sub-delegatee. In case of companies to be listed on the Prime Market, such sub-delegatees are likely to be Remuneration Committees. From such a viewpoint, I think the revised Code could include an additional supplementary principle, which specifies the concept of Remuneration Committee (including an optional committee) that should have sufficient understanding of a principle of designing a directors' remuneration plan and ensure independence and neutrality. As for Nomination Committee, its functions may significantly differ depending on whether it nominates independent director candidates or the management team. Depending on whom it nominates, a necessary organizational structure of Nomination Committee may differ. Especially, when the committee nominates independent director candidates, it is desirable that influence of the management team is eliminated to the greatest possible extent. In other words, Nomination Committee needs to retain a high level of independence. On the other hand, as for the nomination of management team members, closer coordination with business execution may be needed. Therefore, it is considered that an organizational structure of Nomination Committee should differ depending on whether it nominates independent director candidates or management team members. I'd like to have further discussion on this point.

Finally, as my third point, I'd like to suggest that the Corporate Governance Code should include a guiding principle regarding lead directors. In order for Nomination Committee and Remuneration Committee to perform their functions, I believe communications and exchange of information among independent directors are essential. As Mr. Ao reported at the beginning, a lead director can act as a contact point for dialogue with large shareholders, especially institutional investors, or other

stakeholders. I consider that the Corporate Governance Code could define a lead director as a key player in executive sessions and engagement with institutional investors.

These three are what I wanted to share with you. Thank you very much.

[Kanda, Chair] Thank you very much.

Next, Ms. Takayama, please go ahead.

[Takayama, member] This is Takayama. With respect to the topic of the board effectiveness, mainly focusing on the board composition on page 18, I'd like to express my opinion concerning the improvement of the quality and quantity of outside directors.

First, as for the quantity or the number of independent directors, other members referred to one third or a majority. On page 9 of Material 2 concerning governance expected for the Prime Market, discussions at the Expert Study Group on Capital Markets are quoted as excerpts. It shows one idea: "It is considered that the Prime Market adopts certain requirements by many institutional investors in the proxy voting policy/guidelines, including boards comprising one-third independent directors." I'd like to share a supplementary explanation with you.

Currently, looking at proxy voting guidelines of top 10 largest institutional investors in terms of assets under management to invest in Japanese equities, 6 out of 10 investors, in some way, require that there should be at least one-third of independent directors on the board. This is the requirement from the majority of the institutional investors, and their targets include companies without a parent company or a controlling shareholder. Considering such circumstances, in our further discussion, I believe we should be very conscious about the fact that major institutional investors, being large shareholders of Japanese companies, consider the 'one-third' number is very important.

Furthermore, based on the fact that many Japanese companies have already appointed at least one-third of board members as independent directors, I believe that the revised Code should clearly stipulate that it is desirable to have at least one-third of independent directors on the board. If it is difficult to apply it to all companies, such a principle should apply at least to the Prime Market.

Next, I'd like to share my view of 'a majority' with you. I think 'a majority' is desirable in the future. However, before going for it, I believe it is extremely important to enhance the capabilities of independent directors, improving and retaining their quality. I suggest that we should develop an approach to secure the quality of independent directors first, and then discuss 'a majority' issue.

Now I'd like to talk about the improvement of the quality of independent directors. There are

two time points to consider the improvement of quality or capability. One is the time of appointing independent directors, and another time point is after the appointment. I think the ICGN's opinion statement, which Kerri-san explained earlier, serves as a very useful reference. As for the time of appointment, section 3.4.1 of the ICGN's opinion statement provides an explanation on appointment of independent directors. It is stated that board appointments and succession planning should be led by the Nomination Committee. I agree with that. I suggest that the Code should more clearly refer to the process of appointment for independent directors and succession planning as responsibilities of the Nomination Committee and the board.

As for the evaluation after the appointment, the ICGN's opinion statement again serves as a useful reference. Section 3.4.3 of the opinion statement refers to evaluation, which means an board evaluation. It is stated that companies should undertake a review of performance of the board, committees and individual directors, and engage an external consultant to undertake such evaluations. I agree with that. Especially, I support the recommendation about a review of committees, including Nomination Committee, as well as individual directors.

I believe that the Code should contain such details concerning the improvement of the quality of independent directors as I just mentioned. Then who should be subject to such a requirement, all the companies or those to be listed on the Prime Market? Compared to quantitative requirements such as 'one-third', such a qualitative approach would be easier for companies to work on. Therefore, I suggest that it should be applied to all companies, regardless of whether they are listed on the Prime Market or not.

That's all.

[Kanda, Chair] Thank you very much.

Next, Mr. Okada, please go ahead.

[Okada, member] This is Okada. I'd like to make a few comments on the board effectiveness and ensuring diversity. First, as for the number of independent directors, I agree that the majority of the board members should be independent directors. In reality, in most companies, since inside directors constitute a majority of the board, most of board agendas have already been deliberated at the management meeting and conclusions have already been drawn, before the board discusses them. That is the actual situation. In short, there are many cases where discussions at board meetings are merely for the form's sake. In that sense, considering that the board should be a venue where

independent directors freely discuss matters from a critical viewpoint, I believe that independent directors should constitute a majority of the board.

However, in reality, it is true that there are very few independent director candidates. Accordingly, we should not rush to make companies increase the number of independent directors by sticking to 'a majority'. If we stick to 'a majority', there will be possible cases where companies appoint people who satisfy the current independence criteria, but do not have necessary skills – for example, the CEO will bring in his/her friends. Such cases would be unavoidable. In the process of increasing the number of independent directors, it will be necessary to sufficiently verify their actual skills, including the number of years of experience, instead of just looking at 'yes or no' in a skill matrix. I believe it will be an important role of the Nomination Committee.

I earlier referred to the shortage of independent director candidates. One possible reason would be because, in listed companies, independent directors with corporate backgrounds are mostly incumbent presidents/chairpersons of other companies. According to specific characteristics of those from other companies on page 4 of Material 4, roughly one-third of them do not have experience as presidents/chairpersons. Although the percentage is much larger than I expected, it is only a half of the percentage of those with experience as presidents and chairpersons. I presume that companies can find qualified human resources from those with experience as directors, not as presidents/chairpersons. Furthermore, considering the current situation where a single person serves as an independent director of multiple companies, we need a system that companies should appoint more independent directors from those without experience as presidents/chairpersons.

In this connection, although this is just a basis for further discussion, we could require companies to disclose how many retired directors, including retired presidents/chairpersons, remain in their corporate groups, regardless of whether or not remuneration is provided, or regardless of job titles (for example, advisor, corporate consultant, etc.), although we do not require disclosure of names of such persons. Companies should realize that providing human resources capable of serving as independent directors is a part of social contribution. However, I'm concerned about one thing: the current level of remuneration for independent directors is too low. Unless considerable remuneration is provided even if their pre-retirement level of remunerations cannot be guaranteed, they feel it is more advantageous and easier to remain in the group companies in reality.

Another possible reasons for the shortage of independent directors would be a delay in promoting

diversity. Companies seem to be preoccupied with numbers, for example, the number of female independent directors, and the number of foreign independent directors, merely for a positive evaluation by investors. In Japan, I assume that the reason why it is important to include women and foreigners is because they are not bound by traditional hierarchies of Japanese companies. In other words, it is important not to sense and conform to the atmosphere of the boardroom. It is essential for boards to have many members who voice critical opinions without conforming to the atmosphere, and to accept such opinions. As for female independent directors, it is true that some are highly competent and have a high level of awareness as independent directors, but the absolute number of such women is small. Consequently, they serve as independent directors of many companies. It is important to spend a great deal of time to develop qualified women. In addition to companies' own efforts, I hope that investors would also contribute to development of female officers through dialogue. I also expect that women develop themselves by readily facing criticism.

I said foreigners do not sense and conform to the atmosphere of the boardroom. I'd like foreigners to express their opinions in a straightforward manner. For that purpose, it is desirable to increase the number of foreigners on board. Recently, tools for simultaneous translation into English and multiple other languages have been being developed, so I think it is possible to improve communications by refining such tools. On the other hand, again there is an issue of remuneration. I hear that in case of appointing foreign directors in Japan, their remuneration level is very different from that for Japanese directors in some companies. I think this is one of the challenges.

My last point is about Nomination Committee. I've been wondering whether Nomination Committee is really functioning. An increasing number of Nomination Committees comprise a majority of independent directors. However, while CEOs are often to be appointed from among internal human resources, typically inside directors, in Japan, outside directors do not have knowledge about internal human resources. That's the way things are. Then, even if a Nomination Committee deliberates on a proposal submitted by the executive body, I assume that such a deliberation is for the form's sake and the committee is not functioning in a substantial manner.

Therefore, it is desirable that companies provide information on their specific approaches or views, including nomination policies and procedures, in their Corporate Governance Reports. Page 16 of Material 2 from the Japan Exchange Group (JPX) shows an example of disclosure on the "process of formulating/implementing Succession Plan" at the bottom, and the example provides

detailed information. I also think this disclosure method is ideal, but most companies merely disclose that “the appointment of the CEO is considered by the Nomination Committee”. If the Code requires enhanced disclosure, companies consequently need to ensure that their Nomination Committees perform their functions in a substantial manner, I think.

That’s all from me.

[Kanda, Chair] Thank you very much.

Next, Mr. Oguchi, please go ahead.

[Oguchi, member] Thank you. I’d like to make two comments.

My first comment is about “board effectiveness centered on the composition” which is the subject to be discussed (1) on page 18 of the Secretariat’s material. This has been a core issue since the establishment of the Code in 2015. Although this issue was addressed in depth in the revised Code in 2018, even today it remains as the issue to be further discussed. Of course, the underlying reason is the importance and difficulty of this issue. However, given that this issue seems to be less extensively discussed than before in other countries, I assume that other countries may have found certain forms that lead to substance, although it may sound paradoxical when our key phrase of the governance reform is “from form to substance”.

The second bullet point on that page refers to the ratio of independent directors on board, and it is considered to be one of the forms leading to substance. I think independence of board chair is also globally important points as its attributes.

Page 8 shows rules of other countries. In the UK, the board chair should be independent. In Singapore, when the board chair is not independent, a majority of board members are expected to be independent directors. Furthermore, as Kerrie mentioned earlier and also stated in section 3.1.4 of her opinion statement, ICGN has the same stipulation as the UK’s – maybe it is Guidance 2.1 of the ICGN’s Global Governance Principles. These are the basis for global institutional investors for voicing their views through the exercise of voting rights. This way, the effectiveness of independence of board chairs is recognized in other countries. In Japan as well, General Principles 4 of the Code refers to “effective oversight from an independent and objective standpoint” as one of responsibilities of the board. So, there is a concern that the lack of reference to the board chair may appear odd to people in other countries. In the meantime, according to the TSE’s White Paper on Corporate Governance, even among JPX-Nikkei 400 companies, companies with the board chaired by an

independent director account for only 4%. I'm aware of such reality, as well as opinions expressed by other members.

Nevertheless, when companies already have a considerable number of independent directors, their boards can be chaired by independent directors even now, as a part of their initiatives for more effective use of such independent directors. So, for example, we could adopt Singapore method to the Prime Market. Specifically speaking, a board should be chaired by an independent director; and if not, a majority of the board members should be independent directors. We should consider that the revised Code refers to the independence of the board chair this way. I believe this method is applicable also to the US-type boards as mentioned earlier, and matches with the request in the Cabinet decision, that is to "satisfy the interests of the international community while being in alignment with the actual conditions of Japanese businesses."

My next point is about "ensuring diversity", which is the subject to be discussed (2). From the perspective of achieving mid- to long-term sustainability, which is one of the governance issues to be considered for the revision, I believe that companies should work on this issue with a clear awareness.

As I briefly mentioned in the previous meeting, overseas investors are concerned about investing in Japan, a country with aging population and a declining birth rate, from the long-term perspective, and question earnings and spending power. Offering information about how Japanese companies utilize diverse human resources from the mid- to long-term perspective would be one answer to such a concern or question.

However, overseas investors have a deep impression that personnel systems in Japan are very rigid, so an extension of existing information provision will not resonate well with them. Therefore, if the revised Code encourages companies to set measurable targets for assigning women, foreigners, and mid-career hires and disclose such targets and achievements, as mentioned in this Material, such a specific measure unlike traditional Japanese ways will be effective in terms of changing overseas investors' viewpoints of Japan, as well as encouraging transformation of the companies.

That's all from me.

[Kanda, Chair] Thank you very much.

Next, Professor Ikeo, please go ahead.

[Ikeo, member] Thank you.

With respect to the board effectiveness, we've been discussing numbers today. I understand that the discussion on such numbers as a majority or one-third is still important, but it is necessary to discuss the quality at the same time. Especially, I believe setting a tenure limits for independent directors is a key point, as Kerri-san pointed out. It is because the externality will virtually change over time, even if factors of the externality remain unchanged in terms of form. For example, independent directors receive an explanation of agendas from insiders every time prior to board meetings. By repeating such a practice, independent directors are gradually taken in insiders' logic, or understand insiders' logic well. There is such an aspect, so the externality is lost while independent directors are serving for a long time. The externality cannot be secured by itself. It is necessary to make efforts to retain the externality, so I believe it is important for an independent director not to stay in the position too long. In that sense, I agree that companies should disclose their tenure limits.

However, regarding regular evaluations by an external evaluation organization, we face an issue of the lack of such competent external evaluation organizations. Generally, external evaluations are desirable for ensuring the externality. However, if asked whether there are really capable and useful external evaluation organizations in Japan, it is hard to find them at the moment, despite of an extensive research. I'd like to discuss this point during the meeting. In terms of defining independence, it is important to consider a substantive definition, and note the fact that a long tenure may fetter and shackle independent directors.

That's all.

[Kanda, Chair] Thank you very much.

Next, Ms. Matsuoka, please go ahead.

[Matsuoka, member] Thank you.

I'd like to talk about both "board effectiveness centered on the composition" and "ensuring diversity". As for the former, I have nothing special to say from the standpoint of the Chair of the Sub-Committee on Capital Markets of Keidanren (Japan Business Federation), but I'd like to share the situation of my company later.

As for the second subject "ensuring diversity", as other members mentioned earlier, I'm aware that, for business management, diversity is a source of innovation and creation of new value, and a key component of business strategies. In order to further promote corporate reforms after COVID-19, companies are aware that ensuring diversity is essential in terms of governance as well as

corporate management.

On November 9, Keidanren published its proposal “. The NEW Growth Strategy”, which advocates that diversity should be proactively pursued in terms of gender, age, nationality, background, and the existence or non-existence of disability. It also sets a specific target aiming at increasing the percentage of female executives to 30% or more by 2030, and encourages individual companies to take voluntary governance initiatives to ensure diversity.

At the end of October, Keidanren published results of a survey. We found a tendency that companies, which have been earnestly working on flexible workstyles and diversity before COVID-19, can more smoothly ensure business continuity amid COVID-19, including implementation of BCP and continuation of corporate management, as well as effective promotion of sustainability. Many companies responded they are aware that diversity and inclusion is the key to adaptation to the significantly changing business environment after COVID-19, and innovation of new products and services, as well. As such, promoting diversity has steadily become a major trend, so it is important to formulate measures to encourage and support efforts of individual companies.

In order to facilitate such voluntary efforts of individual companies, it would be meaningful to encourage them to disclose their views for ensuring diversity of people with various attributes and backgrounds, including women, foreigners, and mid-career hires, as well as their voluntary targets for promoting diversity. However, I think we need to further consider how the various efforts of companies can be effectively disclosed.

I also believe that it is important to develop the preconditions for seeking human resources with diverse backgrounds and attributes: for example, making the country more comfortable for foreigners with high-level skills to live and work in, and develop social infrastructures and a support system enabling them to work. It would be also indispensable to create a favorable environment in terms of a fluid labor market as well as laws and regulations. Therefore, I'd like the Government unitedly to implement necessary measures and create an environment for enabling companies to ensure diversity, in parallel with such governance initiatives.

I'm going back to the first subject “board effectiveness centered on its composition”. Since other members expressed various opinions, I'd like to share our company's situation with you for your reference. Most of our directors are outside directors, and the board is chaired by an outside director. The executive side, including myself, listens to shareholders' voices, as someone pointed out earlier,

seeks opinions/judgments of the board concerning strategies for business execution and corporate management; and our directors, who are also in the position to represent shareholders, hold very active discussions. In this sense, I believe that our structure is working effectively, with our management and our board which is consisted primarily of outside directors. However, each company has its own background and circumstances, so it would be important to discuss what are feasible and effective mechanisms from a practical perspective.

That's all. Thank you.

[Kanda, Chair] Thank you very much.

I have received chat messages from 9 members, and the remaining time is 27 minutes. Dividing 27 by 9, each speaker has 3 minutes at a maximum. So I have to ask you to make brief comments. I'm sorry for always asking you to do so in the middle of meetings, but I'd appreciate it if you could be time conscious.

Next, Dr. Ueda, please go ahead.

[Ueda, member] Thank you. I'll briefly make comments within 3 minutes.

With respect to board effectiveness, I got an impression that our discussion this time places a disproportionate emphasis on the Prime Market. Certainly, the Prime Market is to be a globally competitive market, and companies need to be aware of being listed on such a market, so it is very important to have discussion on such a premise. On the other hand, as for the Standard Market, it is also necessary to pay careful attention to companies listed on the standard Japanese market. With this in mind, I'd like to briefly make three comments.

My first point is about independent directors. Considering companies' awareness or positioning in the markets I just mentioned, they will be required, as a minimum standard, to have boards comprising at least one-third of independent directors. Furthermore, in case of companies listed on the Prime Market, or in case of parent-subsiary listings, a majority will be required. In addition, in order to make them perform more effectively, I suggest that the Code should clarify the roles of the board chair and the CEO, or refer to such best practices as the introduction of lead directors who are independent directors or a mechanism enabling independent directors to perform their functions. The Code is now in such a stage. Unlike appointing just one or two independent director(s), when companies appoint one-third or a majority of independent directors, they need to consider the quality of independent directors more seriously, including identifying necessary skill sets and developing a

skill matrix. They also need to consider diversity more than before. Therefore, considering that the Corporate Governance Code is meant for leading market segments of the Japanese market, this is a good opportunity to demonstrate that the Japanese market is no more behind in these areas: I think we have entered the next phase to present higher standards.

The next point is about Nomination Committee and Remuneration Committee. Since roughly 60% of companies have already established such committees, we should consider this issue based on the premise that listed companies should establish such committees. As for the composition of the committee members, while Supplementary Principle 4.10.1 of the current Code uses such a vague expression as “independent directors make significant contributions”, it would be better to emphasize the independence by stating that independent directors comprise a majority of the committee, or that the committee is chaired by an outsider. Such a high standard would be accepted as corporate practice is catching up with that.

Finally, with respect to diversity, discussions tend to focus on forms, including attributes, women, foreigners, and mid-career hires, but I believe it is necessary to consider their functions and backgrounds as well. Discussion should be held from the perspective of eliminating the homogeneity and ensuring the heterogeneity. I believe that the skill matrix is necessary in order to show the status to shareholders and investors, and to explain why individual directors are needed for the board.

Furthermore, in addition to gender and nationality, generation or age may be included in the elements. Going forward, the use of human resources and diversity will be topics of dialogues. However, such dialogues will not happen immediately. Companies are expected to share/provide such information as their views/policies, targets, and achievements in a traceable manner, so that shareholders and the market will make positive evaluations of their efforts.

That’s all. Thank you.

[Kanda, Chair] Thank you very much.

Now Mr. Kawakita, it’s your turn.

[Kawakita, member] This is Kawakita. Excuse me for being unable to use video.

As for independent directors, especially those of companies listed on the Prime Market, simply put, I agree with “at least one-third” for the time being, while companies should aim at securing a majority of independent directors in the future.

Next, as for Nomination and Remuneration Committees in connection with the CEO and

independent directors, I agree that the Code includes these matters. I also consider it is necessary to stipulate that a majority of committee members should be independent directors/officers.

As for diversity, in terms of diversifying viewpoints and decision-making of companies, naturally I support such a direction. However, setting higher standards concerning the number or percentage of certain groups of people is too much – it is rather for the formality. Therefore, it is necessary to encourage their substantive efforts as well. And if diversity initiatives of a company lack substance, the company will face a shakeout. In case of companies listed on the Prime Market, they will be delisted. Such measures will be required at the same time.

For that purpose, speaking from the viewpoint of investors, [companies and investors] need to have dialogues concerning, for example, whether or not it is appropriate that a person serves as an outside director of 3 or more companies, as well as the independence issue, and whether [directors and officers] have necessary skills. At the same time, they also need to discuss the performance. To do so, information is required. For example, I believe it is very important to disclose information in English, and provide such information as directors' skill matrix.

In this connection, going forward, it will be essential to secure system-related skills and experience. Conversely, even if a person has experience in corporate management, it will be meaningless if such experience is mediocre. Investors should discuss such a point.

Although this may not be an issue related to the Corporate Governance Code, while some investors vote against certain director candidates of a company, they still continue to include such a company in their index investments. I believe such a practice is problematic, since it is against shakeout from the viewpoint of investors.

I'd like to talk about one more thing, although it is not an issue related to the Corporate Governance Code again. In terms of listing standards of the Prime Market, even if the bar of market cap, which represents an aggregation of investors' valuation, is set at a certain level for the time being, the Stock Exchange should periodically – say, in every 3 years or 5 years – raise the bar in line with the GNP growth. I believe the Stock Exchange should make such efforts, as well as address the issue of parent-subsidary listings, although this is a topic to be discussed at a later time.

As such, I wanted to add the remark that stipulations of the Corporate Governance Code alone are not sufficient, and those who respond to the Code should also make efforts.

That's all.

[Kanda, Chair] Thank you very much.

Now, Mr. Sampei, it's your turn.

[Sampei, member] This is Sampei. Thank you for the opportunity.

I'd like to make a few comments on the board composition and diversity.

With respect to the board composition, as other members mentioned, ultimately the Code may require a majority, but I believe that at the moment, we rather need to emphasize the improvement of the quality.

That said, I'd like to talk a little about the percentage. Although it is not right to set the percentage or number first, I think 'at least one-third' has genuine reasons. Reason No. 1: the objective of introducing independent directors is to avoid possible concentration of authority, to avoid the situation where board members sense and conform to the atmosphere of the boardroom in response to the concentration of authority, and to ensure the effective oversight while outsiders monitor such matters. Reason No. 2: in terms of oversight of potential conflicts of interest with general shareholders, it is necessary to have an independent Nomination Committee and an independent Remuneration Committee to avoid the concentration of authority, and ensure transparency of the decision-making process. On that premise, what is an independent committee? It requires at least two independent directors, and Nomination Committee and Remuneration Committee should be chaired by different persons to avoid the concentration of authority, or the members of both committees should not be exactly the same – some should serve as members of only one of the committees. In doing so, three independent directors are required in total. And, currently, in case of companies listed on the TSE First Section, it is reported that the average board size is 8.9 persons. When 3 independent directors are required as I just explained, three divided eight point nine is roughly one-third. Therefore, 'one-third' has such implications. It's not like the percentage is predetermined. It is important to understand the meaning or purposes of the percentage.

Meanwhile, with respect to the quality, from my experience of talking with many independent directors face-to-face, I'd like to share an illustrative example. There are some persons who used to manage a company before the Corporate Governance Code was established. They maintain their former management styles even when they serve as independent directors and provide advice, and it makes shareholders feel something is wrong. In that sense, I'd like companies to evaluate the effectiveness of committees, especially Nomination Committee. While many other members used

the terms “long-term strategies of companies” and “skill matrix”, I believe that the elements of the skill matrix are important, in terms of checking whether such elements match with the direction of the strategy. A certain company was using different skill matrices for disclosure and the use by the Nomination Committee, like the back of the paper. Its matrix for disclosure was made for affirmative explanations of the current state, and another matrix actually used by the Nomination Committee explores the ideal state. I think all the companies should do the same as the latter practice. However, if there is a huge gap between the ideal state and the current state, I assume they cannot disclose the skill matrix that indicates the absence of necessary skills. So I consider it is necessary for companies to disclose, in their reports of effectiveness evaluations, whether their Nomination Committees are utilizing such matrix to explore the ideal state. I also believe it is necessary to disclose whether or not there were cases where Nomination Committee’s recommendation was not adopted by the board – turned down by the board, and, if any, what was turned down. I believe such effectiveness evaluations are required.

I also think dialogue is an important method to improve the quality of independent directors. We also have dialogue with independent directors. At first, our interactions are somewhat like figuring out a perception gap between us, but at the end of the one-hour meeting, we got along well with each other, and independent directors clearly understood expectations of shareholders and investors. It is necessary to actively accumulate such experience.

Finally, I’d like to talk about ensuring diversity, especially setting measurable targets and disclosing such targets and achievements in the first bullet point. As for women and foreigners, numerical targets may be effective. However, as for mid-career hires, numerical targets are unlikely to work. Especially in case of recruiting external talent at the executive officer level, I don’t think numerical targets are really proper for them. However, it may be valid to disclose objectives, underlying idea, state of utilizing human resources, and a few traceable numerical values. For example, if mid-career hires do not work for a company for a long time, and quit soon, it is problematic. So the numerical information needs to be traceable. There are examples of some companies. A large retailer acquired external talent in order to promote DX, and that person is promoting a new operating model as an executive officer. There are various examples. However, we cannot obtain such information unless we ask the companies, so it would be important to encourage them to proactively disclose such information.

The next one is my last point. As for human resources development and the improvement of the internal environment, it would be necessary to measure the achievement. It is effective to go through the PDCA cycle within the company, and disclose a part of PDCA results, so that shareholders will support such activities. What are achievements here? I think they are revitalization, new idea generation and concept creation. Compared to increasing productivity solely by cost reduction, I believe it is more significant in terms of sustainability and upside. Some companies are already doing that, and some companies have already disclosed such information. I'd like to promote such things.

That's all.

[Kanda, Chair] Thank you very much.

Next, Mr. Haruta, please go ahead.

[Haruta, member] Thank you for the opportunity despite time constraints. I'll briefly make a few comments.

I believe that the effectiveness of independent director is very important. However, listening to today's discussion, I feel the focus tends to be placed on the number or percentage of independent directors, yet I believe what is important is the improvement of the quality. In that sense, I believe it is essential to conduct periodical evaluations regularly according to the appropriate evaluation criteria: if external evaluations are difficult, I think internal evaluations are fine. In conducting such evaluations, it is important to evaluate to what extent independent directors have performed expected roles, and contributed to or were involved in implementing corporate policies. When independent directors are criticized for losing substance, I think such evaluations will contribute to preventing such ineffectiveness.

Furthermore, I believe it is especially important to create an environment that enables outside directors to perform their roles. It is important to develop a mechanism which includes regular dialogue with stakeholders, including labor unions like us, and information sharing with the company they serve. I hope such an arrangement will lead to the effectiveness of independent directors.

Needless to say, I believe it is extremely important to ensure diversity, including sustainability of companies. In this context, I think it is important to disclose such information as corporate policies and targets towards ensuring diversity, achievements in ensuring diversity, human resource development, and improvement of the internal environment; and then incorporate such matters into the ESG indicators, especially those for social factors (S of ESG), and ensure the linkage with the

policy. If that is done in a way to promote diversity in a company, it will lead to sustainability of the society.

I briefly expressed my view. That's all.

[Kanda, Chair] Thank you very much.

Next, it's your turn, Mr. Kobayashi.

[Kobayashi, member] In this rapidly changing world, I believe a new perception of times is required: that is to say, the existing management talent within the company alone cannot achieve a digital transformation or sustainability transformation, or respond to the pandemic and healthcare challenges. In that sense, inevitably, companies are required to seek human resources for not only directors but also executive officers from abroad or different business sectors. We should keep it in mind, when we consider how the board should be constituted.

In Japan, there are three forms of corporate organizations: Company with Three Committees (Nomination, Audit and Remuneration), Company with Supervisory Committee, and Company with *Kansayaku* Board (i.e. Company with Audit & Supervisory Board). And there will be three new market segments, namely, the Prime, Standard, and Growth Markets, in the near future. Under such circumstances, Mitsubishi Chemical Holdings, as a Company with Three Committees aiming at being listed on the Prime Market, has adopted the monitoring board to completely separate business execution and oversight. Currently, the board consists of 5 independent directors and 7 inside directors, but I got an impression that definitions of the terms "inside directors" and "independent directors" are not very clear. In our company, a professor of chemical engineering of University of California, Santa Barbara assumes the position of director. He used to serve as the CEO of our research subsidiary, so he is an inside director according to the existing definition, but he is fully independent in terms of mentality. He looks at things solely from the viewpoint of a global scientist. So I would say he is an "independent inside director". On the contrary, as Professor Ikeo mentioned, when independent directors stay in the positions for a long time, they will become like inside directors. Therefore, I believe that it is more important to consider the definitions for the purpose of increasing the oversight effectiveness, rather than sticking to the externality based on the form.

In addition, non-executive directors, who oversee business execution, do not receive information about day-to-day business execution. So, I would say they maintain their independence in terms of looking at things from a fair and objective viewpoint. For example, while I serve as Chairperson, I'm

not involved in business execution at all. Therefore, while being an inside director, I consider myself as being clearly independent. Perceiving such reality, I believe we should clarify the relationship between the CEO and Chairperson, or between the CEO and board chair.

As for diversity, page 5 of Material 4 shows the skill matrix of our company as an example. Since our company is a pure holding company, the spectrum of talent required for directors is different from that of business corporations in our Group. Mr. Sampei earlier pointed out that it is important to ensure the consistency between strategies and the skill matrix. As for business corporations, required skills are mainly insights into work sites and technologies, including safety and security. As for pure holding companies, required skills should be considered from the perspective of what skills are advantageous for realizing a portfolio transformation.

Next, I'd like to talk about Nomination Committee. Our Nomination Committee consists of five members, specifically, 4 independent directors and 1 inside director; that is myself as Chairperson. Until last year, the CEO was a member of Nomination Committee, so the composition was three independent directors versus two inside directors. From this year, it was decided that the CEO should not be a Committee member, thus creating the situation where independent directors account for an absolute majority. Conversely, it is necessary to create an environment where the Nomination Committee members can familiarize themselves with candidates for evaluations, with the proper collaboration of HR and general administration staff on the executive side to arrange opportunities for independent directors to get to know high-potential human resources, who are candidates for the management team, through their frequent presentations.

With respect to the human resources market for independent directors in Japan, if companies seek only those with experience as presidents and chairpersons, including women, there is not a sufficient number of people. Speaking from my experience, it is extremely useful for managing directors or senior managing directors to serve as independent directors of other companies. It is a great learning opportunity to acquire skills necessary for the CEO. In that sense, I believe that we should consider a broader human resources market. Considering the shortage of female executives, this would be even more important.

In any case, we need to reconsider whether, in this era of SDGs or ESG, sustainable increase in corporate value can be achieved by Japanese people alone. I think we have entered such a phase. In case of our company, the Nomination Committee nominated a Belgian person to be the CEO from

next April. The most important criteria were how much he/she can increase corporate value, and what philosophy he/she has concerning sustainability. When our company sought a person who has such specialty or potentiality most, unfortunately it was not a Japanese person within the company. That is the reality.

That's all.

[Kanda, Chair] Thank you very much.

We have only three minutes left, and there remain four members waiting for their turn. So please keep it in mind. Mr. Takei, please go ahead.

[Takei, member] Thank you.

My first point is about the number of independent directors. In this regard, discussing “one-third” would be only possible if the target were limited to the Prime Market and it were on the ‘Comply or Explain’ basis. However, I believe it is not yet appropriate to require all the companies subject to the Code – including the Standard Market other than the Prime Market – to comply with the requirement to achieve “a majority”.

With regard to independent directors, Mr. Kobayashi mentioned that there may be “independent inside directors”. While the topic of independent directors is discussed here, I’d like to argue that independent human resources are not limited to “directors”: there are independent *kansayaku* (Audit & Supervisory Board members) as well. Despite that, our discussion focuses only on “independent outside directors”. Under such circumstances, if we strengthen disciplines that focus only on the number of independent outside directors, by requiring one-third or a majority, it will result in negating Company with *Kansayaku* Board (Company with Audit & Supervisory Board) itself. As you know, in case of Company with *Kansayaku* Board, the board of directors is characterized as management board, and is required by the Companies Act to serve as a meeting body to make decisions on important matters of business execution. Imagine the situation where half of the members of the meeting body, which makes decisions on business execution, are outsiders. That would negate the organizational form of “Company with *Kansayaku* Board” itself. That said, I think it is difficult to send a message that listed companies in Japan should not adopt the form of Company with *Kansayaku* Board. Therefore, it is difficult to discuss independent directors in a way to expand the scope of application to all the companies subject to the Code, including those listed on the

Standard Market, or to require “a majority”. I’d like to point out that some companies, which adopted the form of Company with *Kansayaku* Board, have created good corporate value in Japan.

In this connection, I’d like to point out that independence is a negative requirement, not a positive requirement. Positive requirements are related to the quality of independent directors and diversity, which other members discussed earlier. Since independence is a negative requirement, emphasizing such a negative requirement may cause an adverse effect, for example, on the quality of independent directors, as someone pointed out earlier. This is my first point.

My second point is related to diversity. I believe that the skill matrix is very important. Basically, companies are expected to recognize their business challenges and sustainability issues, as well as current challenges to respond to DX. Based on such recognition, they are expected to take action in order to become resilient. From such a perspective, they should first disclose their views on diversity necessary for them. It would be meaningful that, only after disclosing such views first, they set and disclose measurable targets and achievements concerning typical matters related to diversity, for example, gender, international insight, mid-career hires, and their presence in managerial positions. This is my second point.

My third point is about the tenure of officers. Long tenure and short tenure – that is also an example of diversity. We should not always consider that long tenure is wrong. As a real-world example, there was a case where a long-serving independent director contributed to preventing a corporate scandal by the top management. If independent directors are replaced all together regularly at certain intervals, it does not ensure the increase of diversity making the company more resilient. In that sense, I believe that the mix of short and long tenures should be regarded as one kind of diversity. This is my third point.

Finally, my fourth point is related to board effectiveness, and active board deliberations. I believe that agenda-setting is important to boards. Regardless of whether a board is chaired by an inside director or an independent director, it is important how agendas of board meetings are set. As for the facilitator function to make board deliberations active, who performs the facilitator function is essential. It is important that the facilitator creates an environment where independent directors provide coaching and ask good questions. Principle 4.12 of the current Corporate Governance Code does not refer to such points, so it is considered that Principle 4.12 stipulates agenda-setting and the facilitator function. In addition, it would be important to refer to the roles of the secretariat for the

board, which support such functions.

That's all.

[Kanda, Chair] Thank you very much.

The next speaker is Mr. Iwama. Please go ahead.

[Iwama, member] Thank you.

Although I feel all sorts of views have been expressed, I'd like to suggest that we could consider the improvement of the quality of boards from the perspective of protecting minority shareholders' interests. For example, votes against a proposal at a general shareholders' meeting accounted for 20 or 30%, how will the board respond to that? The company should disclose its response. By doing so, I think the board will have a keener sense of tension.

From that perspective, while some members discussed whether it is appropriate for a single person to concurrently serve as CEO and chairman, I think it would be effective if an independent director serves as a lead director or performs a similar function, in terms of the interface with shareholders.

With respect to the issue of diversity, while recruitment by companies is shifting to the "job-type employment" [hiring people with skills/experience that match job description], how effectively they use mid-career hires will lead to strengthening workforce capability as well as ability to implement strategies. When it moves ahead, naturally diversity in terms of gender and nationality will increase, and lead to the sustainable increase in corporate value. From that perspective, if individual companies express their approach to this issue, it will lead to active discussions with investors.

That's all. Thank you.

[Kanda, Chair] Thank you very much.

The next speaker is Mr. Tsumuraya. Please go ahead.

[Tsumuraya, member] Thank you. I'll briefly make two points.

First, I agree with the recommendation for companies listed on the Prime Market to have a majority of independent directors on the board. I'm fully aware of the relationship with the forms of corporate organization, and the positioning of *kansayaku* (Audit & Supervisory Board members), but I believe it will become necessary for independent directors to account for a majority of the board so that they will become more responsible, and therefore the quality of independent directors will improve. The era where independent officers are appointed merely because of their independence,

has ended within the past 5 years. That's the reason why I agree with a majority.

According to the results of research by my research office, the average age of independent directors in Japan is higher than the average age of inside directors. It is difficult to put in words, but it was probably because companies appointed those who have very impressive resumes as outside directors. On the other hand, tenures of both inside directors and independent directors in Japan are the shortest in the world. So I think companies could appoint younger people and let them stay for a long time, so that they become familiar with the company they serve, and thus can solve various problems. However, since there is a concern about cozy relationships, one possible direction would be to maintain their sense of tension through disclosure and dialogue. That's my first point.

The second point is related to women and foreigners. From the standpoint of an educator, I'd like companies to disclose the status of recruitment of foreigners. Japanese companies actively use the term "global", but the recruitment of foreign students is very limited, based on first-hand information. Furthermore, the door is shut on foreign students who "deviated from track" in the Japanese sense, for example, senior year students who are older than their peers due to military obligation, etc. Therefore, by disclosing the status of recruitment in advance, I'd like companies to fill the gap from the standpoint of academia.

That's all.

[Kanda, Chair] Thank you very much.

The last speaker is Mr. Oba. Is the Internet connection all right today? Please go ahead.

[Oba, member] This is Oba. Briefly speaking, I believe it is very important to make companies ensure information disclosure stipulated in General Principle 3 of the Code once again, in terms of ensuring the effectiveness. Speaking of an overall impression, there is an achievement in terms of an increase in the number of independent directors, but it is hard to say that it contributed to the ability to deliver added value and sustainable increase in corporate value in Japan. Companies have not disclosed results of board evaluations in this regard. Although board evaluations are very difficult, how they disclose the results of evaluations by themselves and others is very important. This is my first point.

Another point is about individual disclosures. As Mr. Takei also mentioned, each company has different challenges. So, it is very important to disclose the following matters: challenges, the compositions of the board, Nomination Committee, and Remuneration Committee, rationale for such

compositions – to solve which challenges the company appointed them as a portfolio, the objectives of the compositions of the board and committees.

That's all.

[Kanda, Chair] Thank you very much.

I'm sorry that the meeting ran past the scheduled closing time, but I'm glad that all the attendees expressed their opinions. Thank you very much for your invaluable inputs. And thank you for your participation in the online meeting for long hours.

Now I'd like to close today's discussion.

I'd like to ask the Secretariat to make some announcements, if any.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] As for the next meeting date of the Council, we will fix the date, which is convenient for you, and let you know later.

That's all from the Secretariat.

[Kanda, Chair] Thank you very much.

Now I declare the meeting adjourned. Thank you again for your long hours.

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