(Provisional translation)

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

1. Date and Time: January 26, 2021 (Tuesday)　9:30-12:00
2. Venue: 9F, Central Government Building No. 7, Meeting Room

[Kanda, Chair]　Good morning. It's less than a minute to go before the scheduled meeting time, so let's get started. I'm pleased to open the Twenty-Third Council of Experts Meeting Concerning the Follow-up of Japan's Stewardship Code and Corporate Governance Code. Thank you very much to everyone for taking time out of your busy schedule to be with us today.

We will start with an explanation of our two themes, "Group Governance/Shareholding Structure" and "Capital Efficiency/Allocation of Management Resources," from the Secretariat. We will then have a statement from the Tokyo Stock Exchange on the disclosure of group management approaches and policies. After this, I would like to open the floor.

Let's begin with the FSA's explanation of "Group governance/Shareholding structure" and "Capital efficiency/Allocation of management resources."

Mr. Shimazaki, over to you.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA]

I would like to start with an explanation of Material 1, "Group governance/Shareholding structure."

Please turn to page 2. Based on the published opinions from the Follow-up Council in April 2019, we are continuing to review the ideal approach to group governance in terms of protecting general shareholders in so-called listed subsidiaries. That is what we are considering today.

The following is a brief excerpt from the opinion statements. With respect to Japanese corporate group management, it has been pointed out that the appropriate allocation of management resources for the group as a whole, including a review of the business portfolio, and risk management of subsidiaries are not being done properly at the moment. We received written opinions that the independence of the board needs to be strengthened, because of the risk of conflicts of interest at listed subsidiaries between the controlling shareholder and general shareholders.

Please turn to page 3. Since 2014, the number of listed subsidiaries has increased by 77 and the ratio of listed subsidiaries has decreased by 0.6%. Looking at the number of listed companies that have controlling shareholders, the percentage of listed companies with controlling shareholders who hold 30% or more of shares is less than 1% in the U.S and the U.K., about 4% in France and Germany, and about 10.7% at present in Japan.

Please turn to page 5. Here we look at protecting the minority shareholders of listed subsidiaries. Regarding listed subsidiaries, investors have mainly pointed out the risk of conflicts of interest between the parent company and minority shareholders. 78% of listed parent companies say that they "do not often feel" there is a risk of a conflict of interest with their minority shareholders.

In the Ministry of Economy, Trade and Industry's practical guidelines concerning group governance, three specific cases are mentioned where the risk of conflicts of interest between the parent company and the listed subsidiary may arise: direct transactions between the parent company and the subsidiary; transfers or adjustment of businesses between the parent company and the subsidiary; or when the parent company/controlling shareholder makes a listed subsidiary wholly-owned.

Please turn to page 6. With respect to the TSE First Section, according to 2019 data, 43.6% of companies have a board with one third or more independent directors, and 15% of listed subsidiaries. For listed companies that do not have a controlling shareholder, 38.1% have a Remuneration Committee. For unlisted companies or listed companies with an individual controlling shareholder, more than 10% of these respectively have a Remuneration Committee.

On page 7, we have the listing regulations of the TSE. In terms of the protection of minority shareholders, necessary and sufficient timely disclosure is required for any significant transaction between a controlling shareholder of a listed company and the listed company after gathering opinions from non-interested parties to ensure there is no disadvantage to minority shareholders. In terms of the sources of opinion used concerning this regulation, the percentage of independent directors and independent *kansayaku* (Audit & Supervisory Board members) is 64.1%.

Please turn to page 8. In the U.S, the protection of minority shareholders is primarily the remit of the judicial precedents of U.S. corporate law, and in the U.K., it is primarily the remit of prior approval procedures under the Listing Rules. As shown in the table, the Listing Regulations in Japan do not allow transactions that are disadvantageous to minority shareholders, and transactions with

related parties must be disclosed in the business report. In the U.S., preliminary procedures such as approval by a majority of minority shareholders and establishment of a special committee make it easier to determine whether a company has fulfilled its fiduciary duty. In the U.K., regulations include the establishment of legally binding agreements to ensure compliance and the requirement for resolutions at general shareholders' meetings for companies with a premium listing. As mentioned in the Note, in Germany, the protection of minority shareholders is provided by a systematic legal framework for corporate groups. Please refer to the reference materials for more details.

I will now move on to talk about the optimization of group management structures. In terms of optimizing group management, a survey of listed companies conducted by the Ministry of Economy, Trade and Industry (METI) showed that about 70% of the companies had clearly defined management rules and business processes in place to ensure an appropriate framework of decision-making and authority for functioning as a corporate group. 25% of companies had reviewed their awareness of management principles and reported this to management.

Moving onto page 11, based on the opinions of METI's Business Restructuring Study Group and interviews with companies, investors, and experts at the FSA, the feedback we have is that companies are keen to review their business portfolio strategies to develop a business model that fits with the post-COVID-19 environment. In this regard, investors have pointed out that it is important for companies to actively review their business portfolios and to take steps accordingly as a group, primarily through the CEO.

Page 12 looks at risk management of the entire group. One of the issues for the management of a group is that it is important to manage risk across all business units. Therefore it is important for the *kansayaku*, the Supervisory Committee and the Audit Committee to collaborate with and utilize the internal audit department to monitor the entire internal control system.

We have covered the optimization of group management. From page 13, we look at cross-shareholdings. The shareholding ratio for cross-shareholdings is lower than that of the controlling shareholders, but these shares are included here from a governance perspective because they are positioned within the spectrum of shareholdings.

The total number of shares held as cross-shareholdings has been on a downward trend since the mid-2010s. Although cross-shareholdings held by financial institutions are declining, corporate cross-shareholdings still remain at a high level.

I'm now on Page 15. From the viewpoint of substantiating voting rights and improving capital efficiency, there are strong calls from investors for companies to reduce their cross-shareholdings and to explain the rationale of these holdings more clearly. Based on consultations with companies by the FSA, in some companies there needs to be more coordination by the finance department with business partners and different business divisions when considering the reduction of cross-shareholdings.

Next, concerning disclosure of cross-shareholdings in the securities report and the enhancement of the details of this disclosure, we are requesting companies to explain their cross-shareholding policy and method of assessing the rationale of their holdings and to disclose the purpose and effects of each of their shareholdings, based on the revisions to the Cabinet Office Ordinance on this matter in the fiscal year ended March 2019.

On page 17, in terms of cross-shareholdings, we have shown some key points for good disclosure, or examples of what others regard as best practice, to improve disclosure beyond formal compliance with the rules. Cross-shareholdings are referred to in the lower part of the slide. The feedback is that investors and analysts see a large gap between what they view as good disclosure and the current reality. This is summarized here. In terms of good disclosure, the effects of cross-shareholdings as these relate to management strategy are highlighted, as well as the actual cross-shareholding policy and approach to disposal of these shares, along with the approach to assessment of these based on market value and dividends.

On page 18, the opinion of investors and analysts is that disclosure concerning cross-shareholdings is improving but still needs to be better.

Finally on cross-shareholdings, with respect to the tradeable share ratio, which is one of the TSE's listing requirements, we have been taking soundings on this since December last year and have decided to exclude cross-shareholdings from the definition of tradeable shares. This is on page 50 of the reference materials.

Following on from this, please turn to page 19. In terms of the discussion points for this meeting, the following points have been made regarding the status of listed subsidiaries and similar entities. Given recent developments in group management, further consideration should be given to the ways in which a group should protect minority shareholders of listed subsidiaries, for example, through strengthening its governance system. In this instance, it should also be noted that, from the point of

view of a listed subsidiary, having a controlling shareholder also allows it to enjoy the benefits of investment of management resources and supervision by that shareholder.

In addition, concerning group governance, with respect to optimizing group management, it has been pointed out that the key issues are optimal allocation of management resources for the entire group, including a review of the business portfolio, and risk management for subsidiaries.

Based on the above perspectives, how should we think about the following issues related to the shareholding structure, including group governance?

A framework for protecting minority shareholders from controlling shareholders, including the involvement of independent directors at listed subsidiaries and the approach to disclosure. In particular, the role and function of the board of listed companies which is responsible for group management and the approach to cross-shareholdings. Are there any other issues to consider regarding group governance and the shareholding structure?

Following on, I would like to talk about “Capital Efficiency / Allocation of Management Resources” as covered in Material 2. The first page is general remarks. On the second page, in the revision of the Corporate Governance Code in 2018, Principle 5.2 was amended to include the accurate identification of cost of capital, review of the business portfolio, and the allocation of management resources, including investment in fixed assets, R&D and human resources.

Please turn to page 3. In the post-COVID-19 economic society, investors and companies are vocal about the need for a review of business models, including strategies on business portfolios. There are many points to focus on, but there is a particular awareness of the issues related to investment in DX and review of face-to-face business models. There is also feedback that the board should commit to making strategic decisions regarding the business model.

Page 4 shows the spread of company ROEs, with ROE moving up to the right. On the other hand, around 44% of investors see “10% or more” as the preferred ROE target level over the medium to long term. ROE is lower in Japan than in Europe and America, and there is a difference in profit margins in particular.

Please turn to page 6. For management approaches that pay attention to cost of capital, the key indicators that company management should focus on are shown in the diagram on the left. It can be seen from the results of the survey that companies focus on indicators such as profit, sales and profit margins, while investors attach greater importance to indicators such as ROE, ROIC, total return on

equity and cost of capital.

On page 7, the percentage of companies that calculate their own cost of capital increased by about 15% from 2018 to 2019, with around half of the companies now calculating their own cost of capital.

Next, we look at securing management resources. We have outlined various opinions on financial strategy in the post-COVID-19 economic environment based on the interviews we have taken. While some say that they are increasing their holdings of cash in response to the crisis and that it is important to balance cash with investments, some investors say that the key point about cash is to cultivate the ability to generate cash rather than just relying on holding cash.

Page 10 shows a report submitted by Mr. Toyama for this meeting. The data shows that the higher the level of operating cash flow, the higher the investment cash flows and R&D expenses. Therefore cash flow functions as a source of investment.

On page 11, on the original topic of securing management resources, this relates to the discussion on the allocation of management resources, investment in fixed assets, R&D and human resources and intangible assets previously pointed out. On page 12 we show the growth of wages, capital investment and R&D spend of Japanese and U.S. companies as follows. With 1994 = 100, 2019 nominal wages are at 104 for Japan and 139 for the U.S. Capital investment is at 115 for Japan and 333 for the U.S. R&D is at 163 for Japan and 219 for the U.S.

Now please turn to page 13. In terms of important indicators in med- to long-term investment and financial strategy, 62% of investors view human resources investment as important compared to 37% of companies. In terms of reasons why institutional investors focus on information related to human resources, around half cited the expected future growth of companies and the securing of outstanding talent.

On page 14, regarding investment in human resources, there have always been some views that this spend should be regarded as an investment rather than a cost, and after the pandemic I think there is a growing awareness of the importance of investment in human resources.

On page 15, we see that corporate investment in human resources is low compared to other countries, and about 75% of companies are unable or somewhat unable to hire, allocate, or train the human resources necessary to realize their management strategies.

On page 16, we see there are periods when the improvement in labor productivity does not correlate with changes in employee wages, and from 2010 the graph shows that labor share has

declined.

On page 17, we show that with intangible assets increasing as a percentage of market value of U.S companies, and in addition, with the role of intellectual property and intellectual property information becoming more important in ESG investment, there is provisional data that suggests this could have an impact on stock prices.

Next, on page 19, concerning business portfolio strategy, it is pointed out that in order to realize sustainable growth, the funds generated by mature businesses can be used to invest in high-risk growth businesses, and businesses under review for consolidation and revitalization can be sold to raise funds for investment in growth businesses. On this basis, it is important to strategically allocate funds based on the life cycle of such businesses.

On page 20, according to the survey, 45% of companies review their business portfolios "regularly, at least once a year" and 17% of companies review their portfolios, "seldom, if ever." About half of the companies have published the strategy and policy of their business portfolios. On page 21, with respect to board meeting discussions, approximately 2/3 of outside directors, according to this survey, believe there is some kind of an issue with business portfolio strategy at their companies. The percentages for their respective responses, "No concrete initiatives or results", "Not enough discussion" "No discussion" are shown on the slide.

Now please turn to page 22. These are the matters for discussion at this meeting. In terms of cost of capital, while the importance of accurately understanding cost of capital has been pointed out previously, the following perspectives need to be considered in light of the coronavirus crisis. Recognition of the importance of holding cash during a crisis such as the current pandemic, and reviewing approaches to securing and overseeing management resources for future investment (for example, improving cash flow generation, business restructuring initiatives). Next, future investment based on the role of human resources (employees) and the increased value of intellectual property, and constructing a business portfolio that enables the management to anticipate changes in economic and social structures.

Based on the above perspectives, how should we think about the following themes?

Management based on an awareness of cost of capital. Securing management resources. Improving operating cash flow as mentioned earlier, and a policy of holding cash, etc.

Then, in terms of the appropriate allocation of management resources, investment in human

resources, intellectual property and R&D.

We should also mention reviews of business portfolio strategy.

For Material 1 and 2, there are matters to be discussed on the final page. Thank you for listening.

[Kanda, Chair] Thank you very much.

Next, I would like to ask the representative from the Tokyo Stock Exchange to tell us the disclosure of ideas and policies regarding group management. Mr. Ao, over to you.

[Ao, Executive Officer, TSE] I'm Ao from Tokyo Stock Exchange. I would like to add a few comment on Material 3, "Information Disclosure Regarding Listed Companies with Controlling Shareholders," regarding the current framework and future direction of this issue.

Please turn to page 2. TSE has been striving to strengthen corporate disclosure to increase protection of minority shareholders' interests, increase predictability for minority shareholders and investors, and enable them to make informed investment decisions.

Specifically, as the table shows, first of all, listed companies with controlling shareholders are asked to disclose the measures they take to protect minority shareholders when they enter into transactions with controlling shareholders, as well as their policies concerning independence from parent company, and the group management policies at the parent company, along with the details of the agreements related to these.

Furthermore, and this applies not only to listed companies that have a controlling shareholder, but also to listed parent companies, we ask for disclosure of the group management policies, the rationale of having a listed subsidiary based on these policies, measures for ensuring the effectiveness of the corporate governance at the listed subsidiary, and the details of the agreements related to the policies.

On the other hand, in recent years, there have been cases in which it has subsequently come to light that there was an agreement with the controlling shareholder regarding the appointment of directors. There are also some cases where it is not clear how business opportunities and sectors are managed or allocated within the group.

herefore, Tokyo Stock Exchange would like to further strengthen disclosure concerning agreement on corporate governance, policies concerning conflicts of interest as well as supervision and control thereof, and management and allocation of business sectors and opportunities within the group, with controlling shareholders, that is, shareholders who have substantial control.

The following pages are examples of actual disclosure at listed companies. This is a simple summary. Thank you for listening.

[Kanda, Chair] Thank you very much.

Following on from this, we have received opinion statements from Ms. Okina, Mr. Toyama, and Ms. Waring. I would now like to ask the Secretariat to give us a brief overview of these.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA]: First of all, I would like to give a summary of the opinion submitted by Ms. Okina. For group governance, directors should fulfill a supervisory function, engaging in discussion from both growth-oriented and defensive perspectives. With parent-subsidiary listings in particular, Ms. Okina's opinion is that it is important for the reasons for these listings to be discussed by the board and clearly explained to shareholders, as well as the board of the listed subsidiary, from the perspective of protecting minority shareholders to ensure appropriate supervision in situations such as parent company transactions. In addition, although it is preferable that parent-subsidiary listings are eliminated altogether, her opinion is that it is necessary to devise a framework where independent directors play their roles in preventing minority shareholders from being disadvantages during takeover bids.

With respect to business portfolio, Ms. Okina's opinion is that it is important for the board to regularly review their business portfolio based on the medium-term management plan and also to ensure organizational ambidexterity. Outside directors need to provide support to help the group CEO make timely decisions and carry out business restructuring as appropriate. Since the business portfolio varies depending on the business model of the company, listed companies need to be able to clearly explain to investors how they will improve the long-term corporate value of their portfolio and their business model.

Ms. Okina's opinion is that in order to improve competitiveness, the ratio of intangible assets to GDP in Japan, which is low compared to developed countries, needs to be improved. She would like to see an improvement in the disclosure of corporate information regarding investment in human capital and more positive engagement from investors. Also, it is important for companies to improve their low net profit margin which is a factor behind the low ROE of Japanese companies in an international context. Her opinion is that companies need to set targets in terms of effective indicators, such as ROIC, aiming at improving corporate value by linking this with remuneration systems.

Following this, we have the opinion of Mr. Toyama. Regarding the discussion of protecting

minority shareholders, problems arise when a parent company which is the controlling shareholder of a publicly-listed subsidiary exerts management influence, including the exercise of its shareholder rights, for its own benefit. The essence of the problem is conflict of interest that may arise concerning the protection of common interests of shareholders of the subsidiary and interests of minority shareholders. Mr. Toyama's opinion is that controlling shareholders of listed companies should have similar fiduciary responsibilities concerning minority shareholders as the directors. Furthermore, his opinion is that the board of listed companies with controlling shareholders should have a majority of independent directors.

In terms of human resources investment, in the midst of the paradigm shift to the knowledge-based industries and the management of intangible assets, where talent is the source of corporate value creation, the current situation of Japanese companies is highly problematic. In Western companies, most part of high-level human resources investment is dedicated to developing key attributes that can be shared on a cross-company basis or advanced capabilities that are valued by the market, along with the acquisition of advanced knowledge or highly skilled talent. Japanese companies are still focused on lifetime employment and seniority system in terms of their human resource investment. This means that many companies still stick to traditional in-house education, developing an employee base that is only valuable within the context of the company itself under this system. This also has the negative effect of making it harder for the company to implement dynamic restructuring of its business portfolio and functional portfolio that transcend existing company boundaries. Mr. Toyama's opinion is that we should consider such a measure that either the Corporate Governance Code or the Disclosure Guidelines imposes strict disciplines concerning human resources investments and human resources management, and requires them to disclose information that is comparable with other companies from the viewpoint of investors and human resources market inside and outside the company.

Next, we have the opinion of Ms. Waring on page 3. First of all, Ms. Waring's opinion is that, in terms of capital efficiency, it is important to encourage capital allocation to establish a sustainable foundation for the creation of corporate value. She expressed opinions as follows: oversight of capital allocation and capital allocation policy are important responsibilities of the board; the board should explain the rationale of the dividends its proposes; the board's allocation of cash and deposits should be based on achieving an acceptable return for investors while maintaining a sufficient level of

capital and liquidity to manage risk; based on the need to create long-term value by using cash for activities that are in line with the purpose of the company, the board should have a clear fund allocation policy and should clarify its reasons for holding non-core assets.

In terms of mutual shareholdings, investors remain concerned about equal treatment of shareholders and the weakening of management discipline. Ms. Waring's opinion is that with regard to disclosure of cross-shareholdings, since the facilitation of business relationships is not a sufficient basis for a cross-shareholding, companies should be subject to tighter requirements on disclosure, and should clarify the nature of their cross-shareholdings, clearly explain their rationale, explain any initiatives to reduce or terminate any holdings during a specific period and state the monetary value of all their holdings in the English language securities report or on the company website.

Regarding corporate group governance, with respect to obligations for independent officers and fiduciaries, Ms. Waring's opinion is that for listed subsidiaries in Japan, independent directors should make up the majority of the board to ensure there is no infringement of minority shareholder interests. In addition, the duty of due care of a prudent manager of subsidiary directors should be clearly stated. It is also effective to require a clear policy regarding the nomination and appointment process of independent directors and the influence that the parent company has over this process. In her opinion, it is important that boards of group companies clarify the benefits and potential costs of being a part of the group, and provide accurate information to shareholders, and that independent directors monitor the relationship between the parent company and its subsidiaries.

Her opinion is that the parent company should establish strong internal controls that apply across the entire group and a comprehensive governance framework that includes risk management procedures. The contribution of a subsidiary company's objectives to the strategic direction of the entire group should be clearly stated; conflicts of interest concerning directors who concurrently hold positions both at the parent company and a subsidiary need to be carefully managed; finally, if there is a controlling shareholder on the board of the subsidiary, the right to protection of minority shareholders should be clearly stated in the company's articles of incorporation. That's it.

[Kanda, Chair] Thank you very much.

Taking into account these explanations and opinions from those who are not attending today, I'd like to invite you to ask questions or to express your opinion. As explained by the Secretariat, there are points to be discussed today. Specifically, these are on the last page of Materials 1 and 2, that is

page 19 of Material 1 and page 22 of Material 2. I'd appreciate it if you could focus your discussion on these points.

Also, since we were a little short of time at the previous meeting, I don't think we allowed enough time for comments. The topic was general shareholder meetings. If you have any additional comments, particularly those who did not get to speak last time, please feel free to make a comment today.

Please can I ask that each speaker restricts their speaking time to five minutes or less. I understand that Mr. Oba has to leave our meeting early today. Mr. Oba, would you like to speak first?

[Oba, member] Thank you very much. There are a lot of issues here and it is difficult to cover each matter in detail, but I would like to make two points.

The first is the issue of capital efficiency. Since every company is different, I think each company needs to deal with its issues through its own dialogue with its investors. Since we have two Codes emphasizing constructive dialogue, I think it is important for investors to have a more active dialogue with companies about improving capital efficiency depending on the individual circumstances.

However, looking at the data, I feel that companies' awareness of this issue is still focused on scale. I think this is summed up on page 6 by the "focus indicators for management objectives". However, it is clear that for companies, the focus is "scale" and for investors, "efficiency". Therefore, I think it would be a good idea to resolve these issues through dialogue.

The second point is the issue of cross-shareholdings and listed subsidiaries. First of all, there are too many listed subsidiaries in Japan compared to the rest of the world. This needs to improve. Originally, if an asset had value as a capital asset, it would be a wholly-owned subsidiary. If not, then I think that capital allocation theory would recommend that the asset should be sold. Based on this alone, I think there needs to be a discussion on why there are so many listed subsidiaries during the engagement.

Next, cross-shareholdings also fall foul of capital allocation theory, so this is something that needs to be discussed during the engagement.

Those are my two key points. However, since there are a lot of issues to be discussed in terms of the outlook post-COVID-19, there are some additional points that need to be covered. These can be summed up in three key words with respect to the post-COVID-19 outlook: green, digital and healthcare. Speaking very broadly, our resources are finite. That is why it is so important to improve

efficiency. From this perspective, I think it is important for companies and investors to have a constructive dialogue with each other. That's all.

[Kanda, Chair] Mr. Oba, thank you very much.

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

Mr. Tsukuda, over to you.

[Tsukuda, member] This is Tsukuda. I just have one point to make on the management of so-called conflicts of interest and the protection of minority interests in listed subsidiaries.

First, in order to ensure the protection of minority shareholders' interests, I believe there need to be strict requirements for independent directors at listed subsidiaries. I believe that at least one-third of the board, and preferably the majority of the board, should be independent directors.

Independent directors of listed subsidiaries are required to be both independent from the management of the subsidiary company, and independent from the parent company. Therefore in difficult situations they will be required to make tough decisions from the perspective of protecting minority interests. Therefore, it is not just the number of independent directors that needs to be carefully considered, but also their quality.

What should we do to improve their quality? Certainly, I am keen to encourage a constructive dialogue between independent directors and investors at listed subsidiaries. In terms of monitoring conflicts of interest, institutional investors should have more opportunities to directly check with independent directors whether or not they are responding appropriately to the needs of minority shareholders.

That's all I have to say.

[Kanda, Chair] Thank you very much.

Now, based on the order of chat messages received, Mr. Tanaka and Mr. Okada will speak, in that order. Mr. Tanaka, over to you.

[Tanaka Member] This follows on from what Mr. Tsukuda has said. On today's topic, I'd like to make a comment based on my own company.

As it so happens, we completed an acquisition yesterday that was originally announced in August last year. The total value of the acquisition was approximately 1.3 trillion yen after the completion of a 100% joint venture in Asia with Wuthelam Group, part of the Goh family business group, and

the acquisition of the Indonesian business.

The 1.3 trillion yen funds for the acquisition were raised through bank financing of 100 billion yen and a 1.2 trillion yen capital increase through a third-party share allotment to Wuthelam, as a result of which Wuthelam became our parent company with a 58.7% stake. Wuthelam was previously the controlling shareholder with a 39% stake even prior to the transaction. As a result, our company's capital increased from 78.9 billion yen pre-deal to 671.4 billion yen after the deal. I think this has greatly strengthened our company's financial position.

Although this transaction was announced on August 21st , last year, the most important factor in laying the groundwork for the deal was the protection of the minority shareholders. For this reason, for the appointment of nine directors at the general meeting of shareholders in March last year, two-thirds, or six directors, were independent directors, all of whom were experienced business operators and experts. As a result, our board has a high level of independence from the controlling shareholder. The purpose of this was to eliminate the risk of structural conflicts of interest in order to protect minority shareholders.

On top of that, when actually making the acquisition, we decided to establish an Independent committee consisting of three independent directors to make completely sure that minority shareholders were being protected. The three members of this committee were a lawyer, an accountant, and a former investment banker, all of whom have a great deal of practical experience in M&A matters. They were selected on the basis of being experienced executives who understand the importance of protecting minority shareholders.

There followed a rigorous negotiation between Wuthelam and the Independent committee. Based on this, in terms of the acquisition price, it was decided that the deal should increase our company's EPS by 10%. On the basis of the theory that "stock price = PER x EPS," an increase in EPS should lead to a rise in the stock price, which in turn maximizes shareholder value and is to the advantage of minority shareholders.

As a result, our stock price has continued to grow strongly – almost double over the past year, marking the fifth highest rate of stock price increase among listed companies. Our market capitalization is now in excess of 3.7 trillion yen. Since the transaction was completed yesterday, the number of shares will increase by 46%. In theory, the market capitalization of our company also increases by that amount. As a result, our market capitalization, which was 1.8 trillion yen at the start

of last year, will rise to around 4.4 to 4.5 trillion yen.

There are three key points that we focused closely on throughout this deal.

First, it is the minority shareholders, not the controlling shareholder, who determine the share price of the controlled subsidiary. The controlling shareholder holds a certain number of shares, but it is minority shareholders who actually buy or sell the shares and drive the share price.

The second point is that protecting the minority shareholders of the controlling subsidiaries has significant benefits for the controlling shareholder as well.

The third point on the protection of minority shareholders is that we need to be convinced that this protection is put in place not from the perspective of the parent company or its subsidiary, but from the perspective of the minority shareholders of the subsidiary. To that end, Mr. Tsukuda made the point earlier about the kind of independent directors that should be appointed. I think this is very important.

Therefore, on this basis, protecting the interests of the minority shareholders of a listed subsidiary that is controlled by a controlling shareholder is a positive driver for the share price and helps to increase the asset value of the controlling shareholder himself. Considering this link, I think that protecting the interests of the minority shareholders of a listed subsidiary is also a favorable arrangement from the viewpoint of the shareholders of the controlling shareholder.

From a governance perspective, I think that the board of the controlling shareholder of a listed subsidiary has a responsibility to protect the interests of the minority shareholders of the listed subsidiary for the benefit of the shareholders of the controlling shareholder company themselves.

Another point of discussion today is the allocation of management resources. Through this transaction, we have strengthened our financial structure. So from the point of view of investing in and securing human resources, we have announced a 3% pay rise for our staff. This is a difficult time, so I think this is an excellent opportunity to secure our employee base.

This is just one example, but I think it is worth pointing out. That's all.

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

Mr. Okada, over to you.

[Okada, member]

First of all, regarding the issue of listed subsidiaries in group governance, I agree with the comments made by Mr. Tsukuda and Mr. Tanaka. It is clear in the Financial Services Agency's

materials that this applies not just to listed subsidiaries but to any situation similar to a listed subsidiary where there is a shareholder with an overwhelming majority, regardless of whether they own 20% or 30% or whatever. Therefore, I suggest that the term should be changed from “listed subsidiaries” to “listed subsidiaries or the like”.

I recently heard of a case where in a takeover bid where the parent company made a listed company a wholly-owned subsidiary, the offer was examined by a special committee made up of outside directors. Although it agreed with the terms of the bid, the view was that it should be up to the shareholders to decide whether or not to accept the offer. I am slightly skeptical that this was the judgment of the independent directors. Although they are called independent directors, I have to say that they are not really independent if the right to nominate them as directors is held by the parent company. For an independent judgment, I would have thought that the number of independent directors on the board should be 50% or more, in other words a majority.

Second, in terms of the governance of subsidiaries other than listed companies, the original format is to respect the independence of the subsidiaries and to delegate authority. In the past, companies tended to be made subsidiaries because this lowered costs for the parent company. Recently, it has become more important to ensure appropriate treatment for employees and other stakeholders. The parent company and the subsidiary are separate corporate entities, and the directors’ execution of duties and supervisory role are carried out according to each company’s form of corporate organization. Since they are separate corporations, the scope of supervision is limited, no matter if they are directors of the parent company.

On the other hand, with regard to *kansayaku* (Audit & Supervisory Board members), the parent company’s *kansayaku* have the authority to examine the management of subsidiary companies as required. This is also stipulated in the Companies Act. In that sense, there are high expectations for the role of *kansayaku* since they are responsible for monitoring the operations of groups and subsidiaries.

Next, on the topic of cross-shareholdings. As shown in the materials, good progress is being made, but there are still some shareholdings that are very well-established and hard to shift. In my opinion, the attitude of both companies, the shareholder and the investee company, needs to change. The attitude of investee companies still seems to be a desire to have a stable shareholder base in terms of their own general shareholder meetings. I think that agenda items at general meetings should be

narrowed down as much as possible, and more time should be spent on actual discussion at the meetings rather than on explanations.

Also, if the income stream from the cross-shareholding company is only dividends, this will not cover the investment costs and the shareholding cannot be justified in economic terms. Disclosure requirements in the securities report have improved recently, but companies in question just provide explanations that they aim at strengthening business relationships and business development, because it is difficult for them to describe the quantitative effects. My concern is that cross-shareholdings may distort the fair trading of stocks. For example, if companies persist with cross-shareholdings, even if they are not profitable, my worry is that business decisions, for example continuing to own a business, are not made on the basis of economic rationale. There is a limit as to how far disclosure requirements can be tightened, so I would like independent directors in board positions to review this situation carefully. Investors could also encourage large corporations to improve this by having a dialogue with them.

If I could add one point. Based on Japanese accounting standards, it is possible to record a profit on the sale of strategically held shares. Therefore I think unrealized gains on cross-shareholding shares may be viewed as a safety net (booking a profit on disposal to make up for unexpected losses). I think it is also necessary to change accounting standards.

Lastly, on the topic of securing management resources, when it comes to human resources, there is an argument for spending money on mid-career recruitment and training. That is certainly important, but I think the key to developing human resources is the staff evaluation system. I think more attention should be paid to how companies conduct staff evaluation to develop their human resources.

I think that 360 degree or multi-faceted assessments are ideal rather than the traditional one-sided Japanese approach. This is because power harassment and sexual harassment are not so easily identified if staff are only assessed by senior personnel. If you have multi-faceted evaluation, this can be useful for evaluating someone, even for the Nomination Committee. I think it is very important for outside directors of the Nominating Committee to understand someone's personality in this way. It depends on each company's way of thinking, but I think it would be useful to know about methods and ideas for evaluating personnel.

That's all. Thank you very much.

[Kanda, Chair]　Thank you very much.

Next, Mr. Haruta, over to you.

[Haruta, member]　This is Haruta. Thank you very much. I look forward to working with you all again this year.

I would like to discuss the issues of group governance and capital efficiency.

First of all, there have been various opinions on the issue of group governance and the ideal approach to cross-shareholdings. At the time of the revision of the Corporate Governance Code in 2018, it was said that the appropriateness of cross-shareholdings should be verified and that the details of this review should be disclosed. What kind of changes were made by this? I think the results of this need to be verified.

In addition to cross-shareholdings, there are also issues with listed subsidiaries, and it is the role of outside directors that we are discussing here. In verifying what role outside directors have played, I think this is significant in terms of the fulfillment of the role of an outside director. In order to enable outside directors to carry out their proper function, it is important to examine the role that they play, in addition to considering the actual number of outside directors.

On the second point, the issue of capital efficiency, I think one of the factors behind the slump in the Japanese economy is that Japanese companies tend not to reinvest their retained earnings. During the pandemic, my concern is that the notion that retained earnings should not be reinvested has gained further credence, based on the corporate mindset of always needing to be prepared in the event of an emergency.

In that sense, I think it is important to understand how retained earnings can be used for investment. We talked about digitalization, going green and healthcare earlier. As companies develop growth strategies in these areas, they need to realize the importance of investment to achieve these goals. I think it is important to be aware of this in connection with policies such as holding cash and deposits in reserve.

I think it is important for outside directors to fulfill a role in this respect as well. Ideally, the Corporate Governance Code should be revised so as to incorporate this perspective into companies' long-term strategy.

In addition, concerning investment in human resources, I think this is the most important issue for us as workers. As with the fields of digitalization, green issues and energy, it is critical to develop

human resources who can respond to the anticipated transformation of industrial structures. As you can see from the presentation materials, the current situation is that investors are very focused on human resources development, and companies less so. In the context of the importance of investment in human resources, it is especially important to increase labor share. In addition to raising wages, training is also important for the development of human resources who are capable of responding to structural changes in industry. I think that in future Japanese companies should be required to focus more on training, including vocational training.

From the standpoint of workers, it is of course important for each employee to have an awareness of training. But I think it is equally important for companies themselves to reach out to their employees. It is important to understand how workers and management can work together in response to the COVID-19 crisis and also in the post-COVID environment. I hope that the Corporate Governance Code supports this dialogue.

That's all I have to say.

[Kanda, Chair] Thank you very much.

Next, Mr. Oguchi, over to you.

[Oguchi, member] Thank you very much. Today's discussion is very broad, but there are a number of interlinked themes here. First of all, I would like to start with the cost of capital. On page 2 of Material 2 which was discussed earlier, in the revision of the Code in 2018 in Principle 5.2, accurate identification of company's cost of capital and the allocation of management resources is referred to, including reviewing the business portfolio and investments in fixed assets, R&D and human resources.

As Mr. Tanaka stated earlier, the response varies from company to company. As a general point or a macro point. If Principle 5.2 is put into practice, I think that the results of this and the resulting return on equity or ROE will improve towards overseas levels, specifically European and U.S. levels, although it will take time to come through.

However, let's look at the data on page 5 of Material 2, which I think is the same as the data presented at the Twentieth meeting. Compared with 2014 when the Stewardship Code was introduced in the bottom table, or even when compared with the Western standards shown in the table at the top, there is still no evidence of significant improvement. Leverage has also deteriorated somewhat since 2014.

So, on page 6 of the material, as pointed out Mr. Oba, as a general remark, although it is companies that implement Principle 5.2, the chart on the left shows that companies themselves do not place as much importance on so-called balance sheet indicators such as ROE, ROIC, total return ratio, and cost of capital. If companies are not focused on their balance sheet, it follows on naturally that the related indicators, including ROE, do not improve as much as investors expect them to. In that case, I would like to see investors engaging with companies and companies' responding to the expectations of investors in principle.

However, from the viewpoint of the company, Mr. Tanaka's comments earlier were very valuable. It wouldn't be an issue if this kind of thinking was widely shared by management. However, I wonder if the reason why companies often don't prioritize balance sheet matters is because they don't actually need to. It's difficult to specify the simple reasonbut I wonder if one of the main influences here is the peculiar stockholding framework in Japan.

As shown on page 3 of Material 1, the percentage of listed companies that have controlling shareholders with stakes of 30% or more in the U.S. and U.K. is less than 1%, while Japan is an outlier with 10%. Then, if you jump to page 14, this page shows cross-shareholdings. The trend is that cross-shareholdings held by financial institutions have certainly decreased as a result of various initiatives, but that cross-shareholdings held by corporations have remained at a high level.

We are discussing the reason why controlling shareholders or strategic shareholders [i.e. cross-shareholders] hold listed stocks. Because these reasons differ from those of general shareholders who are purely seeking investment returns, we have been focused on improving disclosure. However, in the case of listed companies that have such shareholders as controlling shareholders or strategic holders, their focus on general shareholders may be diminished. Just asking controlling shareholders and strategic shareholders to explain the rationale of holding these shares in terms of contribution to profits is not sufficient, since such explanations lack considerations to the common interests of shareholders and the perspective of general shareholders. Therefore I do not think it is a promising approach.

If controlling shareholders and strategic shareholders are asked to contribute to common shareholder interests just as institutional investors and general shareholders, then for their own part I think they will become more aware of the importance of Principle 5.2.

Therefore, I think it is necessary for controlling shareholders and strategic shareholders to assume

responsibility as pure investors, in other words to have stewardship responsibility, as a condition for continuing to hold listed stocks. This should include disclosure of how they exercise voting rights on an individual agenda. If they find it difficult to assume responsibility as pure investors contributing to the common interests of shareholders as stated above, they should be encouraged to sell their holdings.

This may sound a bit blunt, but in the end, I am concerned that without resolving the peculiar shareholding structure of the Japanese market, where controlling shareholders and strategic shareholders with different motivations to general shareholders continue to hold a considerable number of shares, general shareholders will continue to suffer a minority discount, which will in turn continue to adversely affect the valuation of the Japanese market. That's the viewpoint I would like to express.

Furthermore, when it comes to controlling shareholders, their logic concerning capital works by themselves, so it is necessary to be more aware of the need to protect minority shareholders. Therefore, I am in favor of the idea of strengthening the role of independent directors in listed subsidiaries, which many members referred to today. However, no matter how independent the directors of a listed subsidiary are, it is still the controlling shareholder who appoints these directors. So this does not work unless the controlling shareholder is given the role of protecting the minority shareholders of the subsidiary. Specifically, Mr. Toyama's opinion earlier referred to the ratio of independent directors. For controlling shareholders, one approach is for the majority of directors to be independent directors. Or, for the same purpose, establish a voluntary committee, mainly comprising independent directors with responsibility for minority shareholders, such as a Governance Committee, similar to Nomination or Remuneration Committees, to encourage the supervision of conflicts of interest from an independent standpoint.

Last but not least, it may have sounded as if the sole reason why Principle 5.2 has not been put into practice so far were a shareholding structure that is peculiar to Japan. Of course, this is not the only reason. As is also mentioned in the reference materials, low-profit business segments and conglomerate discounts tend to be ignored as shown on the conglomerate discounts page. It could also be that institutional investors, who have a role to engage with these long-term issues and promote improvement together with the companies, are not playing a sufficient part here. I would like to add that I think this is a factor that makes it difficult to resolve the issue.

I apologize for having spoken for so long. That's it.

[Kanda, Chair] Thank you very much.

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

[Sampei, member] This is Sampei. Thank you. There are numerous issues to discuss, but I will try to touch on as many as possible.

First of all, regarding the shareholding structure, as many have commented earlier, how to establish a framework for the protection of minority shareholders from controlling shareholders is a very important issue, and has already been discussed at length in Japan. In short, I believe the problem to be that publicly listed companies fail to protect minority shareholders due to a hole in the system. In 2019, there were several events that raised serious concerns in this respect. In light of this, I think the matter needs to be dealt with as soon as possible.

In this context, as Mr. Oguchi mentioned, I think it is also important to consider the fiduciary duty owed to other shareholders by the parent company that is the controlling shareholder, as well as forms of discipline to be implemented at listed subsidiaries, such as having independent directors constituting the majority of the board. Specifically, this problem pertains to Principles 4.8, 4.3, 4.11 and other parts of the Corporate Governance Code.

So what should we do about it? Coming up with answers to this question has always been difficult. Nevertheless, in such cases, I think it would be desirable to impose a fiduciary duty owed to other shareholders on the parent company that is the controlling shareholder. There is, however, the problem of whether this can be done through the Code. There is also the issue of whether to require listed subsidiaries to have a majority of independent directors even in cases where the controlling shareholder bears fiduciary duty towards the other shareholders – in other words, whether both are needed at the same time.

So, for example, listed subsidiaries may not be required to have a majority of independent directors if the controlling shareholder publishes a declaration that it will fulfill its fiduciary duty to other shareholders. However, in cases where it is unclear whether the controlling shareholder is fulfilling its fiduciary duty to other shareholders, it may be reasonable to see it as the listed subsidiary's responsibility to ensure that a majority of independent directors are appointed in order to protect minority shareholders. This is a similar balancing act to that seen in the United States.

In terms of the Code, the appointment of a majority of independent directors would constitute

compliance on part of the subsidiary. If, on the other hand, a subsidiary were not to appoint a majority of independent directors, I believe it would need to confirm that the controlling shareholder has published a declaration of fulfillment of fiduciary duty to other shareholders. I think this may serve as an explanation.

How, then, should we deal with any violations of fiduciary duty to other shareholders committed by the controlling shareholder? One possible solution is that if the controlling shareholder is, for example, a company required to submit Securities Reports, it may provide a guarantee by including a declaration of fulfillment of fiduciary duty toward other shareholders in its Securities Reports. If the company then fails to fulfill its duty as stated in its Securities Reports, I believe it may be held liable for misrepresentation. In this way, I think we need to consider both the responsibility of controlling shareholders and the responsibility of the listed subsidiaries together, and to think about the balance to be struck in order to achieve our objectives.

I think this approach is necessary because, as Mr. Tanaka mentioned earlier, when both parent and subsidiary companies seek to strike the right balance, protecting the rights of the minority shareholders of listed subsidiaries is not necessarily to the detriment of the controlling shareholder, but rather is aligned with the goals of both parties. Burdening companies with excessive requirements will only result in greater costs for all involved, so I think the best way to go about it may be to provide some sort of incentive or options for companies to consider such steps proactively. This is the first point I wanted to make.

The second issue I wish to discuss is that of cross-shareholdings. Following the TSE's change of the way in which tradable shares are calculated, we are currently seeing a further decrease in cross-shareholdings. In a sense, this behavior contradicts the previous narrative that companies need to hold stock in each other in order to do business. Companies are letting go of the stock now that they want to be listed on the Prime Market, which makes one wonder what the reason for cross-shareholdings was in the first place, and I am not sure that there was a valid one at all.

Also, Principle 1.4 concerning cross-shareholdings refers to assessing the relevance compared to the cost of capital. Right now, however, companies are merely verifying and comparing percentages of economic return and cost of capital. Holding the risk asset of cross-shareholdings means allocating shareholders' equity as a risk buffer and bearing the burden of that amount. Boards are failing to sufficiently recognize and verify this, which is a problem. In this sense, I am concerned that

Supplementary Principle 4.11.3 is probably not being implemented successfully.

Cross-shareholdings sometimes include capital alliances. In such cases, the verification method may be slightly different, but what is more significant about capital alliances is that there is no disclosure whatsoever of the agreements that are likely to be in place with the other party on the terms of the stock transfer, etc. I think disclosing such information is subject to an explanation requirement. I think that cases of failure to disclose the terms of such agreements, which may have a significant impact on investors' decisions, would require strict monitoring, taking into account potential violations of the Securities Listing Regulations.

The third point I would like to make is about the Other Issues raised. As mentioned earlier about controlling shareholders, I think it is necessary to expand their scope to include shareholders that play a controlling role in practice. This is the case based on the actual state of affairs. The threshold for a shareholder to become controlling may be, for example, 25% when considering special resolutions at general shareholders' meetings, or 20% if the company is an equity method affiliate and is recognized as a subsidiary.

In addition, if an agreement of some sort with the controlling shareholder is in place, I think the terms of that agreement should also be disclosed. Only then can the minority shareholders of the subsidiary make an informed decision, which I think is an important point for shareholders and investors.

Lastly, I'd like to touch on a point mentioned in relation to capital efficiency. With regard to promoting the review of business portfolio strategies, I will not go into detail, but the Practical Guidelines for Business Transformations state that in addition to reviewing the basic policy on business portfolio at least once a year, it is the board's responsibility to oversee corporate executives' implementation of business portfolio management and disclose its status. This means that this information should always be reported under Principle 4.11 and disclosed under Principle 5.2 of the Corporate Governance Code.

In such cases, when complying with Principle 5.2, I think companies will need to specify the disclosure points in their Corporate Governance Reports. For example, companies that claim to be in compliance with all items have given vague answers in previous dialogue when asked how they explain the items in Principle 5.2 ("I think it was somewhere in the Integrated Report," or "I think I saw this somewhere"). "I think I saw this somewhere" is not enough. I would like them to state in

their Corporate Governance Reports at least where such information is available.

That's all from me.

[Kanda, Chair] Thank you very much.

The next speaker is Dr. Ueda. Please go ahead.

[Ueda, member] Thank you.

Today's topics may be diverse, but I believe they share the same underlying issues — that is, the meaning of listing, or an awareness of the use of the market functions through which capital is raised. I think we are entering an era where Japanese companies will need to once again recognize these issues, and today's topics were presented in this regard. I thought capital efficiency would come first, but I am going to start by commenting on group governance in accordance with the order set out by the Secretariat.

I think it's excellent that the TSE is discussing the relatively broad concept of controlling shareholders, rather than the narrow concept of group governance and parent-subsidiary listings. Mr. Tanaka expressed a highly proactive view as a corporate manager when he stated that his company is taking minor shareholders into consideration because they are the ones who create the stock price. I think that subsidiaries, first of all, should use the Code to once again recognize the importance of protecting minor shareholders.

There are several points to consider in this respect. The first pertains to related party transactions. I think this is also mentioned in the OECD Principles, etc., but such transactions are not necessarily limited to goods and services. For example, it may be necessary to disclose the transfer of funds, such as low-interest loans of cash and deposits held by a subsidiary within the group. Also, from a governance perspective, I think the role of outside directors is important. I think subsidiaries or controlled companies will need a majority of outside directors who are independent of the parent company.

In fact, I think page 6 of the document mentions that the governance structure of subsidiaries lags behind that of general listed companies. Therefore, in order to ensure independence and the protection of the minority shareholders of subsidiaries, I think it may be reasonable to make firm demands for subsidiaries to establish a Remuneration Committee or Nomination Committee consisting of a majority of independent directors.

Parent companies and controlling shareholders, on the other hand, should probably clarify how

they are taking into consideration the minority shareholders of their subsidiaries. This issue is also linked to the improvement of corporate value across the group and the interests of the parent company's shareholders, and involves a revision of the business portfolio. I think such points should be considered.

Then, with regard to cross-shareholdings, the definition of tradable shares issued by the TSE at the end of last year is very broad, and we use this definition in our analysis to cover a broad range of shares. I think this is a very proactive approach from the market's standpoint, and one that is likely to lead to strict discipline for companies.

As mentioned in this document, the problem is that companies are concerned that they may be unable to get their counterparties to sell their cross-shareholdings. Rather than addressing this problem with the Code or other rules, I think it might be a matter of changing commercial practices themselves. In this respect, it would be desirable to make this known by making substantial revisions to the Code, etc.

I believe that most corporate managers are aware of the problem of cross-shareholdings. Why, then, does the issue persist? It has been pointed out that this is linked to voting rights at general shareholder meetings, and that the department in charge of general meetings warns that the unwinding of cross-shareholdings may cause an impact on voting results at general meetings. This makes it hard for managers to solve the issue.

This highlights the importance of changing the awareness of those in charge of general meetings within the company. In many cases, Corporate Governance Reports and other documents are prepared by staff in charge of general meetings. Therefore, I believe that we need to strongly encourage a change of attitude not only among corporate executives, but also among staff from such departments within companies.

I'm dragging on a bit here, but I'd like to discuss capital efficiency. As mentioned by other members, the issue of capital efficiency is one that we would like to resolve through dialogue rather than through the Code. Therefore, if there are plans to revise the guidelines for dialogue in the future, I hope that capital efficiency will be discussed there. What is particularly important is how aware companies are of their ability to generate cash, as also mentioned in other items for discussion in the materials. I believe this area needs to be thoroughly strengthened.

Also, the materials included an analysis by using DuPont decomposition, which shows low

corporate margins. This has been pointed out for a while now, and I assume that the current goal of companies is to increase the scale of sales rather than profitability at all costs.

In fact, when I read and analyze the Integrated Reports of several companies, I find that many of them focus on sales in their disclosures, even though the information sought by investors and the market is on profitability. I think companies may need to disclose information in this area and provide the information that investors want. In the case of internal resource allocation, however, I think there are cases where resources are allocated based on sales scale rather than profitability. Therefore, in addition to such internal management indexes, I think it will be necessary to once again review indexes that are to be explained to the public in a manner that ensures consistency.

Finally, I would like companies to rethink the significance of listing – including, among other things, the question of whether companies understand the required capital, which precedes discussions of cost of capital. The reason why we are so strict with listed companies is that investors are providing them with equity, which is a risk asset, and are relying solely on the management to get their investment back. In this respect, I think it will be necessary to continue raising awareness through the Code.

That's all from me. Thank you.

[Kanda, Chair] Thank you very much.

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

[Kobayashi, member] I came in at 10:35, so I have missed some explanations and discussions thus far. That said, I would like to discuss my impressions of the materials I received beforehand concerning two points: group management and corporate value, including capital efficiency.

First of all, I think there are quite a few different ways of thinking about group management depending on company category and sector. I have lived my life as a manager at a general chemical company — a typical example of conglomerate discount, especially in Japan where the chemical industry is highly fragmented. It has been a journey of how to transform a company that was originally very heavy, from the old oil- and coal-based chemical products measured in tons to pharmaceuticals measured in micrograms, and eventually to IT- and AI- based service businesses. Looking back over the past decade or so, I think the key to group management in Japan lies in how to discard companies with various businesses, and at the same time, how to incorporate companies with new businesses through M&As. In order to achieve this kind of dynamism, for example, a

holding company system could be adopted, integrating subsidiaries into the group in a "gather round" fashion, and the holding company would be responsible for all the subsidiaries. Otherwise, moving forward would be difficult in practice. A company-to-company merger will cause one brand, one company name and one president to disappear, making it difficult to achieve consolidation.

In that sense, a model where a company is incorporated into a holding company for the time being and a decision is then taken on whether to set the shareholding ratio at 100% or zero is one possible option in terms of corporate transformation, even though listed companies are much more numerous here compared with Europe and America. For example, with this method a shareholding ratio of 50%+ would not be changed until five or ten years have passed under the agreement, but a decision would subsequently be taken to set the ratio to zero or 100%. I think it is important to create this sort of transient space where companies can have the option of setting the percentage to zero or 100%.

In my company's case, we have been repeating a process of discarding and incorporating: we acquired 100% of the equity method subsidiaries of business corporations such as Nippon Kasei and Nippon Synthetic Chemical Industry via TOB; we incorporated Mitsubishi Rayon as a 100% subsidiary directly under [Mitsubishi Chemical] Holdings, and then merged it with other operating companies after a transitional period; and we acquired 100% of Mitsubishi Tanabe Pharma Corporation, in which we used to have a more than 50% stake, via TOB. Currently, our only listed subsidiary at over 50% is Nippon Sanso Holdings, which we incorporated in 2014.

In this process, when we acquired 100% of Mitsubishi Tanabe Pharma, an independent committee took charge of share price valuation. Nippon Sanso Holdings is a very independent company, and to put it bluntly, as far as I can see, they do not just do as the holding company says; on the contrary, although they are our subsidiary, their execution of business is much more robust than ours. The reality is that each industry and each case are different. Therefore, while allowing for transient listed subsidiaries as a way of accelerating transformation, I feel that it is better to have one-third or a majority of independent directors to protect minority shareholders, although I do not think that the Western way of doing things is always correct. I believe that deciding flexibly on either 100% or zero over a period of several years is a good, practical way to promote consolidation in Japan, where we are experiencing excessive competition due to too many companies.

My next point is about corporate value, and I personally think that the key to this is who will

judge the existence of companies as legal entities. In this sense, in addition to capital efficiency and the equity spread (return on equity minus cost of equity), important elements of corporate value also include the type of technology and innovation provided to society. I think the fact that digital transformation and virtual tech companies like GAFA have increased their market capitalization so much is a perfect example of this. In addition to the above, I think that the social and public nature of the company — CSR as it was called in the past, or ESG investment and SDGs as it is called now — and carbon neutrality going forward, as well as concrete contributions to such issues, will also be quite important. Therefore, I feel that we are entering an era in which it is extremely important to be able to demonstrate comprehensive corporate value through narratives like Integrated Reports.

In that sense, with regard to portfolio transformation as well, it feels as though it will also be important to explain, in numerical terms, a weighting 70–80% from the perspective of capital efficiency and equity spread, and another 20–30% from the perspective of social factors like ESG and technological factors promoting carbon neutrality and digital transformation.

The Secretariat's materials show that companies with very large operating cash flows also have large investment cash flows and R&D expenses, and their market capitalization appears to be large as well. It will be important to have discussions based on cash flow as well as P/L and B/S, and I also feel that share prices are likely to express corporate value quite well.

In addition, GDP is no longer necessarily a direct measure of people's wellbeing, especially now that consumer surplus and economic activity can no longer be monitored in the virtual online space. In the future, I think the key will be for corporate entities such as ours, which have hitherto focused on manufacturing, to work on creating new value based on carbon neutrality, and to clearly assert such corporate value.

That's all from me.

[Kanda, Chair] Thank you very much. The next speaker is Mr. Kansaku. Please go ahead.

[Kansaku, member] Thank you.

First of all, I would like to express my opinion on group governance. I think would be desirable to consider taking a head-on approach to all group companies in the Corporate Governance Code. This is because, given the actual state of investing and the consolidation-centered structure of the Financial Instruments and Exchange Act, I believe it would be appropriate to take a step forward in discussing group companies.

For example, the board of a company that controls a group of companies should be responsible for the management of all group companies; it is also worth considering the possibility of specifying in the Governance Code that a corporate group strategy should be formulated as part of the management strategy, and that such a strategy should be implemented without fail. In particular, from the perspective of protective corporate governance, compliance with laws and regulations should be achieved at the level of group companies. I believe that such outcomes should be aimed for as principles, and that monitoring at group level will be extremely important.

In order to achieve this, it will be a prerequisite to establish systems and frameworks where important information about the corporate group is provided to the supervising and monitoring departments in a timely, appropriate and comprehensive manner. I think that such matters could also be included in the Governance Code.

Furthermore, from the perspective of growth-oriented corporate governance, I believe it will be particularly important to review strategies for the business portfolio and the allocation of management resources at the group level.

Today, the Secretariat has discussed the state of affairs in different foreign countries, and Germany, too has a corporate governance code in place. Germany's governance code makes a clear and conscious distinction between provisions that apply to single companies and those that apply to group companies, and uses different terminology for each. I think this may be useful as reference to us in Japan when we think about how to ensure that our Governance Code takes into account entire groups of companies.

When we approach group companies head-on, this inevitably creates an even greater need to examine controlling shareholders and minority shareholders in more detail. Securing and protecting the rights of minority shareholders is already mentioned in the current General Principle 1 and item (iv) of Principle 4.7 of the Governance Code, while controlling shareholders are mentioned in Principle 4.3 and items (iii) and (iv) of Principle 4.7. All of these mentions, however, are very short, concise and general. It seems to me that the Principles should be presented in a more specific fashion while remaining within the principles' framework. In particular, if there are minority shareholders, the interests of minority shareholders may be sacrificed for the interests of the controlling shareholder or the group as a whole. In order to ensure that such risks do not materialize, I think it would be good to consider suggesting best practices in a more in-depth manner to provide adequate

protection for minority shareholders.

Specifically, as a first means to this end, it is extremely important that the members of the organization that have the authority to participate in the formulation of management strategies and decisions on internal control systems, and especially the general outline of the internal control system at the group level, i.e., the members of the board of the controlling company, include people who are independent of the controlling shareholder and consider the interests of minority shareholders. For listed companies with a controlling shareholder, the need to do so is likely even greater. Therefore, with such companies in mind, I think it is possible to provide more specific principles regarding, for example, the ratio of outside directors and their duties and roles with a view to protecting minority shareholders.

Secondly, transactions between group companies are divided into routine and unusual transactions. Routine transactions are supervised with the internal control system at the group level. Unusual transactions — in particular, transactions involving control rights, squeeze-outs, and the allocation of business opportunities and management resources — exert a very large impact on the protection of minor shareholders. Therefore, it would be ideal to be able to document best practices for ensuring the fairness of such transactions and conduct, with a focus on procedural rules, etc., while independent directors play central role in doing so.

Furthermore, it would be desirable to have directors on the board who are independent of the controlling shareholder, especially at the audit and supervisory level, as well as at the head of the Audit Committee and Remuneration Committee, which play important roles in determining remuneration. Moreover, speaking of controlling shareholders, it would be appropriate to clarify that independence from the controlling shareholder includes not only the controlling shareholder itself, but also parties with close capital, personal and business relationships with the controlling shareholder.

Lastly, I would like to say a few words on capital efficiency and the allocation of management resources. In particular, as several members have already mentioned, I too believe that business portfolio strategy is one of the most important issues in light of the current situation of Japanese companies.

Along with spontaneous, internal discussions by the board, I would very much like to see stewardship activities by institutional investors encourage the board to discuss and decide on

business portfolio strategies. I believe it would be desirable for the institutional investors' awareness of the issues to be shared with management in the course of dialogue between the two, and for the issues to be discussed by the board. For example, I think the suggestion made earlier that the board of directors regularly discuss the business portfolio as a best practice is a very good one, as it will make it easier for stewardship activities to lead to discussions of the business portfolio and allocation of management resources at board meetings.

I have dragged on a little, but that is all from me. Thank you.

[Kanda, Chair] Thank you very much.

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

[Tsumuraya, member] Thank you. I would like to briefly make three points. The first point is about group governance, the second about cross-shareholdings, and the third about capital policy.

First off, each member has expressed their own opinion on group governance, but I'd like to point out something that has not yet been touched upon — namely, I think it might be good to give feedback from minority shareholders a little more visibility. So for example, let us say that the percentage of votes for and against, excluding the parent company, etc. is disclosed at the general shareholder meeting. Then, agenda items that have a high ratio of votes against could undergo cause analysis and disclosure. In view, among other things, of the application of Supplementary Principle 1.1.1, such measures may be used to give some more visibility to the opinions of minor shareholders. This is my point about group governance.

Secondly, with regard to cross-shareholdings, as mentioned earlier by Mr. Sampei, the sell-off will move forward if cross-shareholdings are excluded from tradable shares. And if that's the case, I too wonder what the rationale for cross-shareholdings was in the first place.

So I would like to make two suggestions about how to move forward. Firstly, we are seeing some cases of companies stating that they cannot describe the benefits of ownership in their Securities Reports due to trade secrets. I think one way to address this is to have an independent director carry out a thorough check and, on that basis, provide a declaration in their own words to the effect that there is a reason for the cross-shareholding.

In fact, comments by outside directors are included in all Integrated Reports, and Integrated Reports have already been disclosed by more than 500 companies. So I think it would be a good idea to have a section in Corporate Governance (CG) Reports where independent directors can state their

opinions. I think it may be appropriate to set up a space in there for them to express their opinions about cross-shareholdings and capital policies, which I will discuss later.

As for the second specific point, according to my laboratory's research, unilateral shareholdings have been greatly reduced, while cross-shareholdings have remained relatively unchanged. So, in the case of cross-shareholdings, the problem arises when one party wants to sell but the other party asks them not to. For this reason, I think Supplementary Principle 1.4.1 should require companies to internally establish a rule whereby they cannot stop the other party from selling, etc. if it wishes to do so, and that this rule should be made a disclosure item in the CG Report, which I don't think is currently the case.

For example, there are instances where even though a holding company may not prevent such sales, this is not the case with its affiliated business corporations. I think it might be good to revise [Supplementary Principle 1.4.1] so that both listed companies and their group companies are required to establish and disclose such rules. So this is my second point concerning cross-shareholdings.

Finally, with regard to capital policy, while I do think that technical discussion of the likes of CAPM and WACC may be necessary as an overview before deciding on how to go about specific revisions, if we start from there, managers may just disclose calculated figures while actually thinking otherwise, and this would be an issue. Capital cost-conscious management is first of all intended to meet the expectations of shareholders, and I would like everyone to think about how to meet these expectations in the short, medium and long term in terms of risk-return. The first prerequisite is to have such things in place, although naturally liquidity on hand and shareholder returns must also be taken into consideration.

I have two specific proposals to get managers to think about how to meet shareholder expectations. The first is to make both Principle 1.3 and Principle 5.2 disclosure items in CG Reports. Once these are fully disclosed, managers are likely to think about these issues more seriously than before and to state as much, so I would suggest making both Principle 1.3 and Principle 5.2 disclosure items in CG Reports.

In the CG Report, I would like outside directors to explain in their own words how capital policy is being discussed at board meetings. As mentioned earlier with regard to cross-shareholdings, I think it might be advisable to create a section for this.

Moving on to my second specific suggestion, we need to consider whether the company has a

system in place to enable such discussions and disclosures, and in this respect, it is first of all important to have inside and outside directors who are capable of discussing such matters. First of all, with regard to outside directors, Principle 4.11 currently states that at least one *kansayaku* (Audit & Supervisory Board member) must have knowledge of finance and accounting. I think this should apply not only to *kansayaku* but to both *kansayaku* and directors. The words "finance" and "accounting" used here also inevitably make one think of accounting and bookkeeping. Instead, I would like Principle 4.11 to require the presence of outside directors with sufficient expertise not only in accounting and finance, but also capital policy.

Next, with regard to inside directors, I think it may be advisable to add a requirement to consider how to provide a space for learning skills related to capital policy in the training not only of the CEO, but of other executives as well, and disclose this information as far as possible.

That's all from me. Thank you.

[Kanda, Chair] Thank you very much.

The next speaker is Ms. Takayama. Please go ahead.

[Takayama, member] This is Takayama. I would like to offer my opinion on the optimization of group management. A number of opinions on this matter have been voiced from the perspective of listed subsidiaries. However, I would rather express my opinion from the standpoint of listed companies in general and the issues they face instead of listed subsidiaries only. Then, since this meeting is intended to discuss the Corporate Governance Code, I would like to talk about how boards can supervise and support group management.

I believe that the board of a holding company is, in particular, required to adopt the perspective of supervising group management. The board of a holding company is expected to discuss the allocation of management resources across the entire group, including the review of its business portfolio. However, having spoken with members of the boards of various holding companies, I have found that this is not always the case.

For example, in the case of holding companies where the revenue of a specific business subsidiary accounts for a large portion of the total revenue, discussions at the holding company tended to veer toward the subsidiary in question. In some cases, the board of the holdings company was not always able to discuss overall optimization, and instead focused on specific cases. As a result, there was no clear qualitative difference between the board of the holdings company and the board

of its operating subsidiary.

This may eventually be solved by the growth of other business companies, or may be a transitional phenomenon. Some holding companies, however, are struggling with this issue. It is difficult to solve this type of situation, but I think it is important for the board to always be aware of the need to think about group-wide optimization.

Next, I would like to talk about the means we have at our disposal to encourage boards to discuss overall optimization.

One such means is dialogue between investors and the board, which you have already discussed. There is a reason why I said "dialogue between investors and the board" rather than "dialogue between investors and the company." In the context of dialogue between investors and companies, dialogue between investors and management has a long history and has been going on for quite some time. This form of dialogue pertains primarily to investor relations. By contrast, I believe that dialogue with the board will be necessary to understand how the board oversights the optimization of group management and takes its decisions. Specifically, this means dialogue between outside directors and investors.

Both companies and investors are still in a process of trial and error, and there is some hesitation on the part of companies. However, I think it is important that we continue to put pressure on companies in this regard, and that we create an environment where dialogue between investors and outside directors can make further progress.

Another thing is that listed companies have set up a yearly opportunity to review and evaluate the effectiveness of the board. In such situations, many companies verify technical issues such as time allocation and content of documents. However, I think it might be good to use such opportunities for board verification and evaluation to discuss not only such technical issues, but also essential issues such as the ideal role and composition of the board of companies and holding companies.

In turn, I believe that such discussions will lead to the question of what kind of debates should be held at board meetings of this sort, and how the board should be composed in order to have such discussions. The role of the board is likely to become clearer as a result. I think it is important to ask companies to conduct and disclose such evaluations and verifications.

That's all from me.

[Kanda, Chair] Thank you very much. Next, Mr. Kawakita has asked the Secretariat if he could

make a comment. Mr. Kawakita, if you would.

[Kawakita, member] Apologies for not sending the chat message to all participants.

For my part, I would like to talk about group governance, especially in the case of subsidiaries in parent-subsidiary listings, where minority shareholders sell options for the management of subsidiaries to the parent company. I think that this, in turn, causes the share price of subsidiaries to remain low. Whether to take full control at 100%, sell down to 0%, or, as is often seen now, hold about 40% is left to the parent company's discretion. From the point of view of minority shareholders, especially individual shareholders, this makes for a very uncertain investment, regardless of whether they are aware that the company is a subsidiary. I think we should keep this in mind.

From this point of view, and especially from the perspective of subsidiaries, I think it would be good to make an addition to the Code, stating that the dissolution of parent-subsidiary listings would be desirable or something similar. Of course, a decision to maintain a parent-subsidiary listing may be explained, and the corporate group is likely to have a rationale in doing so. Therefore, I think it will be important for parent companies to explain the necessity of any subsidiary listings, and, further, to disclose the direction they intend to take with the listings in the future.

On the other hand, from the subsidiary's point of view, there must be advantages and disadvantages to the presence of the parent company, and I think that both of these should be disclosed. Also, as mentioned by some committee members, I think it will be important to have a system in place to prevent the parent company from forcing unreasonable management — for example, by increasing the ratio of outside directors to a majority.

In addition, my personal opinion is that in the case of a parent-subsidiary listing, the subsidiary should, in principle, be removed from the stock price index and from the newly composed TOPIX.

Secondly, on the related subject of cross-shareholdings, I would like to see more proactive disclosure of the reasons for holding shares in other listed companies. In addition, I think it is necessary to disclose advantages and disadvantages for the companies whose shares are being held. I believe that disclosure from both sides will help us make progress with the dissolution of cross-shareholdings. In this respect, many listed companies have less than 10% or 20% of their shares held, and I think this also applies to cases where a controlling company is present as a shareholder.

As for the third point I would like to make, I think it is natural for the management to calculate the cost of capital for the entire company and for each division when considering the business

portfolio. Of course, there are many ways to calculate the cost of capital, and there is no one right way to do it. However, I think it would be negligent of the management not to calculate or keep in mind the cost of capital in some form. Outside directors are there for this purpose and should point out these issues.

I think some of the members of the Council have raised the issue of dialogue with investors in this regard. A useful reference is "Capital Cost Management for Higher Corporate Value," edited by the Securities Analysts Association of Japan and published last summer. This contains examples of dialogue between investors and companies, such as discussions of cost of capital by sector or approaches to business portfolios. I hope that company managers will read this document, and that investors will also find it useful, as it will give them an idea of how dialogue actually works.

Then, in terms of management resources and especially human resources, the average Japanese company has hitherto been able to secure profits by controlling labor costs — in other words, by lowering the labor share. I believe this was mentioned in the materials also. I think there was some data that showed that increased ROE, but a large part of that increase has been achieved by controlling labor costs, which I think is very negative in terms of future corporate growth and growth conducive to greater added value.

So I believe that companies will need to adopt a broader perspective ensuring that they pay appropriate wages to their personnel and invest in their education, thereby creating a virtuous cycle for management and the economy. At the same time, it will be important to ensure that personnel can work comfortably by expanding telework, reducing commuting time, and taking other measures appropriate to the COVID-19 era.

That's all from me.

[Kanda, Chair] Thank you very much.

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

[Takei, member] This is Takei. Thank you.

First, I'd like to make a point related to general shareholder meetings, which was the topic of the last meeting. In terms of accessibility to shareholders and electronic voting, there has been some talk about electronic voting, especially by institutional investors, but I think it is also important for individual shareholders to be able to exercise their voting rights electronically. For example, voting rights may be exercised not only by mail, but also with smartphones — an area in which the cases

of voting via smartphone have significantly increased since last year. I think it may be worth mentioning a trend toward making electronic voting the default. This is the first point I wanted to make.

The second point pertains to parent-subsidiary listings, which is a very difficult issue. I will call the parent company "P company" for "parent," and the listed subsidiary "S company" for "subsidiary." I believe there are two possible approaches: one is to have the S company enforce discipline, and the other is to have the P company do so.

In the approach where the S company enforces discipline, the advantage is that the S company is a listed company, so in a sense, the P company is within the S company's reach even if it is an undisclosed controlling shareholder, and regardless of whether it is listed or not. In connection with this approach focusing on the S company, there has been talk of appointing outside directors who are also independent of the P company as the majority of the S company's board, but I believe that this might be excessive. In the case of the unusual transactions mentioned earlier by Mr. Kansaku — namely, unusual transactions where there is a conflict of interest between P and S and some level of accountability is required, I think it would be good to involve a number of outside directors of the S company who are also independent of the P company. Beyond that, I think it would indeed be excessive to have all agenda items involving decisions regarding the S company be made by a majority of people who are independent of the P company. Theoretically speaking, the discipline of appointing independent directors originally emerged as a way to expand governance in situations where shareholders are dispersed to some extent. In the case of a parent-subsidiary listing, or when the P company holds a block of shares, the P company will have its own motives and incentives to supervise the S company. Overemphasizing independence from the P company may be detrimental, and may even prevent the P company from exercising its governance over the S company. If the majority of the board of directors of the S company are independent of the P company, the outside directors, who are all independent of the P company, will have a majority vote and determine almost all of the S company's important decisions and agenda items. I think there is a risk that this may undermine the various functions and advantages of governance exerted by the P company. In the U.S., for example, S companies with a controlling shareholder are exempt from the requirement to have a nominating committee in place. In this global context, I think we should consider how to strike a balance with governance exerted by the P company. Setting unusual transactions aside, I

think we can stop at the involvement of independent directors of the S company who are independent of the P company.

Moving on to the next point, there are various problems and issues to be mentioned regarding parent-subsidiary listings in view of the current state of affairs, but as many of you have mentioned earlier, the definition of tradable shares will change drastically this time around, although public comment on the matter is still under way. Based on this current proposed definition, S companies in the Prime Market will probably be few to begin with. In other words, the current situation will change drastically in the next year or two, so we should take that into consideration. I feel as though it would be a mistake to see this as a problem and change the system just because of the current situation.

To add one more thing, since last time we have been talking about how independent directors should account for one third of the board at companies in the Prime Market. Even for the Standard Market, however, a possible approach may be to reduce the number of independent directors to one-third for an S company with a controlling shareholder. If we say, however, that the step after having outside directors account for one third of the board is to have them account for the majority, I am concerned that a range of governance rules implemented by the P company may be diluted as a result.

Also, thus far I have spoken about the approach to take from the S company's perspective. On the other hand, in terms of approaches for P companies to enforce discipline, given that the Governance Code mentions P companies, we need to discuss cases in which P companies are listed companies. There is also the topic of the fiduciary duty of P companies, and there may be examples of governance codes that cover this overseas. In view of the governance role fulfilled by P companies, which was mentioned earlier, I also have misgivings about placing too many restrictions on P companies. Since fiduciary duty is a rather vague concept, if we were to write something, I think it would be fine to state that the P company must not interfere with the interests of the S company's general shareholders. If, however, we include a broad description of fiduciary duty, care should be taken lest the P company itself should hesitate in enforcing a range of governance rules on the S company. Company P is a listed company, and has its own general shareholders. This is what I had to say with regard to parent-subsidiary listings.

My third point is about cross-shareholdings. This point is somewhat similar to those made earlier, and I believe that the situation will change completely in the future as the definition of tradable shares undergoes a drastic change. In short, shares under 10% that used to be tradable shares unless they

were held by officers, etc. and are currently held by domestic commercial banks, insurance companies and business companies will virtually all become fixed stock instead of tradable shares. The definition of tradable shares has changed significantly to require 35% of shares for the prime market and 25% of shares for the standard market. The effects of these measures will become apparent in the next year or two. In our discussion, I think it would be better to avoid overemphasizing various problems perceived based on the current state of affairs. As a matter of fact, this change in the definition of tradable shares is likely to have a substantial effect. Therefore, I think we may want to give it some thought before we take any steps based on the current state of affairs, which precedes such changes. As mentioned earlier by Mr. Oba, there may be a range of other options in addition to the Code, including various dialogue. At least, however, the Governance Code already contains considerably in-depth provisions of this issue. The situation is going to change going forward, and I think we should consider whether further changes in the Governance Code of this issue is necessary, taking into account that the effect of the definition of tradable shares on the reform of market structure will be considerable. This is what I had to say about cross-shareholdings.

Fourthly, I would like to emphasize the vital importance of business portfolios. The Ministry of Economy, Trade and Industry (METI) has also pointed out in its Practical Guidelines for Business Reorganization that we should shift away from absolute value and scale and toward ratios. As mentioned earlier about internal KPIs, I think this is an important issue that needs to be fully addressed, including how to set up internal KPIs.

Lastly, I would like to talk about human capital investment, intellectual property investment and R&D investment. This point is also very important, as it relates to the ability to generate cash flow as well as sustainability. I think Section 2 should adequately cover human capital investment, intellectual property investment strategy and R&D investment. I would also like it to touch on the importance of investing human capital in personnel who are responsible for defensive governance. The people who are in charge of preventions or preventive governance are the ones who don't have the sales figures, as is the case, for example, at legal affairs departments, and I think human investment in these types of people is now vital. Therefore, I think it would be a good idea to write about human capital investment in the context of sustainability in Section 2.

That's all from me.

[Kanda, Chair] Thank you very much.

Mr. Iwama, it seems like you had tried to say something with the "raise your hand" function. My apologies if that was the case. Please let us know your thoughts, if any.

[Iwama, member] Thank you.

This is more my impression than anything, but with regard to the issue of listed subsidiaries, as some of you have pointed out, I view the current form of shareholding as part of a transitional situation. However, given that we are talking about listed subsidiaries, as remarked by Mr. Tanaka, a framework should be firmly in place to ensure that the emphasis on the interests of minority shareholders creates an overall virtuous circle. In this sense, the attitude of the parent company's board and its composition are very important, so I think the role of independent directors is a vital one.

I think the development of business strategy, the transformation of the business portfolio and cross-shareholdings are all interrelated. In particular, when it comes to shifting the composition of business portfolios, the type of human resources required will depend on the type of strategy implemented. I think the best way to procure the necessary human resources would be to provide on-the-job training within the company, or to source human resources from outside the company if they are not available within it. When it comes to sourcing from outside the company, the liquidity of the human resources market is an extremely important issue. I think we need to broaden the framework of how we look at the labor market in the future instead of just looking at changes to the Governance Code.

A number of points have also been made with regard to cross-shareholdings. Basically, it will no longer be appropriate to simply hold cross-shareholdings tacitly: companies will likely have to explain their strategic significance, and in such a way that investors can clearly determine whether the strategy is appropriate. In this regard, I think it may be necessary to bolster disclosure further.

Generally, I think the issues that have been discussed are very important for making the Corporate Governance Code substantially better in the future, and I agree with the basic direction outlined.

That's all from me.

[Kanda, Chair] Thank you very much. In that case, the only member who is present and participating today and has not yet made a statement is Mr. Obata of NEC. Mr. Obata, please go ahead if you would like to add anything.

[Obata, member] Thank you. This is Obata from NEC. Sorry I'm late to join.

I agree with the basic direction outlined. Since we have listed companies in our group, we take care to ensure that the interests of minority shareholders are not harmed, and we tend to be especially strict when it comes to parent-subsidiary listings. On the other hand, if we take this approach, as Mr. Takei mentioned earlier, the parent company's governance may become less effective in some respects.

Therefore, for listed subsidiaries, I believe that each company has its own requirements. I think it would be good if a system preventing harm to the interests of minority shareholders, which is a concern, could be established by properly implementing various mechanisms.

I agree with everyone's comments on other issues such as business portfolios and cost of capital, so I have nothing in particular to add.

That's all from me. Thank you.

[Kanda, Chair] Thank you very much.

I'm glad that all the attendees have expressed their opinions today. Does anyone have any additional comments? No? If that's the case, it's a little early, but I'd like to close today's discussion now, although I may ask for extensions in the future.

Finally, if the Secretariat has any announcements to make, please go ahead.

[Shimazaki, Director of the Corporate Accounting and Disclosure Division, FSA] We will be finalizing the date of the next Follow-up Council meeting, taking into account everyone's availability, and will be in touch about this at a later time.

That's all from the Secretariat. Thank you for your time today.

[Kanda, Chair] Thank you very much for your invaluable comments today.

I now declare today's meeting adjourned. Thank you.

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