

**27th Meeting of the Council of Experts Concerning the Follow-up of
Japan's Stewardship Code and Japan's Corporate Governance Code**

1. Date and Time: May 16, 2022 (Monday) 9:00-11:30
2. Venue: This meeting was organized virtually.

[Kanda, Chair] Good morning, everyone. Thank you for your participation. I'd like to start today's meeting of the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code. This is the twenty-seventh meeting. It's been a long time since we last met, and I'd like to thank you for taking time out of your busy schedules to join us.

Today, the members are participating in the meeting online. The meeting is also being livestreamed. Minutes will be prepared and published on the website of the Financial Services Agency (FSA) as usual at a later date. Thank you for your understanding.

I will be using headphones today. Please let me know if you have any difficulty hearing me.

I'd like to start by asking the Secretariat to introduce two new members who joined the Follow-up Council. Director Hirokawa, please go ahead.

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

I'm Hirokawa from the Corporate Accounting and Disclosure Division at the Financial Services Agency, serving on the secretariat of the Council. It is my pleasure to be working with you.

I would like to introduce two new members of the Follow-up Council and ask them to say a few words. The first new member is Mr. Toshiaki Higashihara. Please go ahead and introduce yourself.

[Higashihara, member] Good morning, everybody. I am participating for the first time today, my name is Higashihara and I work for Hitachi, Ltd. I have served as a director for the past eight years. As you know, Hitachi has been implementing a number of director-related reforms since the time when Mr. Kawamura and Mr. Nakanishi were in charge, and I too have been involved in these reforms during the past eight years.

Viewed in this light, Hitachi currently has a total of 13 directors. Of these, only three have a relationship with Hitachi. The executives are me (the chairman), the president, and one former officer, and we are the three Hitachi-related personnel. The other 10 members are from outside the company, 6 of these 10 are not Japanese. So this is our board composition, and given that Hitachi is a 'Company with Three Committees', the nomination committee, remuneration committee, and audit committee are all

chaired by outside directors. The chairman of the Board is also an outside director, and so we are now operating in such a way that Hitachi's executive and governance functions are relatively separate.

When I became president in around 2014, there were slight differences between the documents distributed to executives (the management) and the documents distributed to directors, but now we distribute exactly the same documents to both inside and outside directors. In this sense, I believe that we are being consistent in the way that we share information with directors and the management. Something we are particularly focusing on is how to establish a common understanding of the vision of the future of Hitachi and what the management is currently doing toward achieving the vision.

Looking at the governance of the board of directors in Europe and the U.S., directors play a very strong role in governance. Yet, in Hitachi, the autonomy of the management has also been increasingly asserted, so we are striking a good balance between the governance of the board of directors and the autonomy of the management. In this sense, mutual trust and confidence are very important, and that is an area of our focus.

One of the characteristics of Hitachi's board members is that many of them are passionate about educating candidates for executive positions, who will lead Hitachi in the future, and the members frequently conduct activities for that purpose, including training for executive candidates. In terms of ensuring diversity, we have been training female leaders, and we are starting to see female board members taking on role model positions. In addition, we are increasingly seeing cases where directors are mentoring executives whom they consider to have further growth potential. In this sense, I believe that our board members and executives trust each other and have meaningful discussions about the future of the company.

That's all from me.

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

Thank you very much, Mr. Higashihara.

Now, let's move on to the other new member, Mr. Takahito Katayama. Mr. Katayama, please go ahead.

[Katayama, member] My name is Katayama from the Japanese Trade Union Confederation. Pleased to meet you. I was appointed Director of Economic and Social Policy Division last October. I am honored to be working with you all.

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

Thank you very much, Mr. Katayama.

As for continuing members and observers, please check the list we distributed to you. Furthermore, there were some changes in personnel of the secretariat, but due to time constraints, rather than introducing those changes to you now, I ask that you look at the seating chart for details.

That's all from me.

[Kanda, Chair] Thank you very much. We will now move on to the agenda.

Today, the secretariat, specifically, the FSA and the Tokyo Stock Exchange, will first explain the materials, and then we will have time for questions, answers and discussion.

First, the representative of the FSA will provide explanations. Director Hirokawa, please go ahead.

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

Thank you. I am going to explain in the explanatory materials [Material No. 2] prepared by the secretariat that you have in front of you.

Please turn to the table of contents on page 1. There are two items on today's agenda. The first item is the interim review following the 2021 revision of the Corporate Governance Code, and the second item is specific issues, more specifically, challenges for sustainable growth and issues related to dialogue between companies and investors. I will now briefly explain the materials.

Please turn to page 2. First, I would like to talk about the interim review following the revision of the Corporate Governance Code. Since the formulation of Stewardship Code in 2014, a series of corporate governance reforms have been implemented. Following the 2021 revision of the Corporate Governance Code, companies have made progress in their efforts to reform corporate governance systems. For example, as of April 2022, more than 80% of the companies listed on the Prime Market have at least one-third independent directors. And nearly 80% of companies listed on the Prime Market have established nomination committees, and more than 80% have established remuneration committees.

Please turn to page 3. While these reforms are making progress, the following points have also been brought to our attention. For example, companies have pointed out that although the Code adopted the "comply or explain" approach, in practice, companies are concerned about whether investors will fully understand if they choose to "explain". Moreover, consideration process for such explanation is cumbersome. Under such circumstances, in some cases, responses to the Code may become formalistic. Furthermore, companies have pointed out that there is a need to verify whether the revision of the Code and governance reforms of Japanese companies have led to improvements in corporate value and "earning power".

On the other hand, institutional investors have pointed out the need for further reforms, including institutional elements that support constructive engagement with companies. They have suggested that companies should consider further utilization of cash and retained earnings to achieve sustainable growth.

As part of the review, we have compiled results of empirical research with the help of Professor Tsumuraya. The FSA has also interviewed companies. As stated at the bottom, the main focus of the

review, was the initiatives by listed companies to enhance and strengthen governance and engagement, and the innovative approaches being made by companies and the challenges they are facing.

Please turn to page 5. Regarding empirical research, there has been an accumulation of empirical research overseas on the conditions under which corporate performance is affected by the development of corporate governance systems and shareholdings by institutional investors. Please see page 6 for details. On the other hand, there are not that many empirical studies covering the period after the implementation of Japan's corporate governance reforms, and the results of such studies are varied. It would seem that the evaluation of reforms in empirical studies in Japan has not necessarily reached a conclusion yet.

For example, let me introduce an example from one of the studies in relation to outside directors. A study that covered the period before the reforms were implemented, concluded that the introduction of outside directors increased the market's evaluation of the company. On the other hand, although several studies have been conducted after the reforms were implemented, a large percentage of them have found no significant relationship between the appointment of outside directors and corporate value. Regarding the establishment of committees, research has shown that companies with a nomination committee and remuneration committee have higher ROA growth. With respect to capital policy, reducing excess cash and cash equivalents increases the market's valuation. As for cross-shareholdings, unwinding cross-shareholdings improves profit margins, and increases share buybacks and dividends. There is a research paper that shows a significant relationship between these. With regard to dialogue or engagement, there is a research paper on how engagement with institutional investors leads to better governance and higher stock prices. With respect to stock ownership, the higher the active investor ratio, the higher the R&D outcome in the manufacturing sector. And research has shown that companies with higher ratios of institutional investors and foreign ownership have higher productivity and market evaluations.

I will now move on to talk about page 16, which shows the overview of the corporate interviews we conducted. We interviewed 16 listed companies between December of last year and April of this year. The Keidanren (Japan Business Federation) cooperated with us in the selection of the target companies. I would like to take this opportunity to thank everyone for their cooperation. The names of the individual companies we interviewed are listed on this page.

Moving on to page 17, I would like to share with you some of what we heard from companies during the interviews. First, as you can see from the key takeaways section at the top, the main evaluation of corporate governance reform is that many companies, including the management side, pointed out that enhanced deliberations on the board and deepened discussions on medium- and long-term business strategies had a positive impact on their business, and that dialogue with investors has yielded useful

suggestions for management. We feel that this suggests that the direction and effectiveness of corporate governance reforms are widely supported. For example, as is written at the bottom, with regard to boards fulfilling their functions, we heard many stories about various efforts being taken such as coming up with creative ways for executives to explain things.

Regarding the key issues that were pointed out, the first one being that as companies are under pressure to comply, there are concerns that the Corporate Governance Code's requirements for details of corporate management may result in merely formalistic responses by companies, thus making the reforms insubstantial. The second issue raised is that higher quality engagement should be promoted by addressing issues such as the merely formal exercise of voting rights by institutional investors, and the lack of opportunities for engagement at medium or smaller sized companies in particular and difficulties in identifying substantial shareholders.

I would also like to introduce some excerpts from the bottom of the page. A company reported that its board discusses medium- to long-term business strategies, delegates authority to executives, and then monitors the progress of the execution; and such an approach has increased the speed of decision-making and implementation, and enabled business management in line with mid- to long-term strategies. As for board effectiveness evaluations, we received comments that applying the PDCA cycle to their corporate governance reform through the evaluation of board effectiveness has led to an improvement in the quality of the board.

Lastly, with regard to engagement, we received positive feedback stating that their presidents, board chairmen, and outside directors are actively and continuously engaged in dialogue, and that they gained useful suggestions through dialogue with investors, who view them from a medium- to long-term perspective.

Skipping through the materials, there are two main specific issues, the first being the issue of sustainable growth.

As you will see if you turn to page 23, corporate governance reform aims to support management's decisive risk-taking to enhance corporate value over the medium- to long-term, but we believe that Japanese companies' investment in growth (capital investment, R&D/IP investment, human resources investment, etc.) has increased only modestly since the Corporate Governance Code was formulated. The line graph at the bottom of the slide is a macro statistic, so it is important to keep that in mind.

Turning to page 24, following the revision of Corporate Governance Code, during this past year, we believe that discussions on the allocation of management resources to intellectual property and human capital have been taking place in the Cabinet Secretariat, the Ministry of Economy, Trade and Industry,

and outside of the government in various forms. However, at this point in time, the results of surveys indicate that, companies do not seem to have yet fully recognized the importance of this issue compared with investors.

Turning next to page 25, currently, large Japanese companies have accumulated retained earnings of 242 trillion yen, and cash and deposits of 79 trillion yen. You can see several charts at the bottom of the page. From the perspective of growth investment, there is a need to pay a certain amount of attention as to how this is reflected in accounting practice. For example, let's look at salary and benefits in relation to human capital, and R&D expenses in relation to R&D and intellectual property. As shown in the middle of the chart, such expenses are included in the profit and loss statement as expenses for the current fiscal year, and current net income will decrease accordingly. Then what matters is how this will lead to increased corporate value in the future. Furthermore, a certain portion of current net income, which is not used for dividend payments and share buybacks as shown on the right, accumulates as retained earnings on the balance sheet. Retained earnings are entered on the credit side. In the context of growth investment, for example, if a company invests in capital equipment or conducts an M&A, the retained earnings will not be reduced, and the impact will be seen in the form of assets on the debit side. In such a situation, we understand that there may be issues such as how to consider cash and deposits on the debit side.

I will now move on to page 26. Share buybacks is something that is often discussed. Looking at the level of shareholder returns, the data shows that dividends and share buybacks by Japanese companies are not necessarily excessive compared to the United States and the United Kingdom.

Moving on, I would like to explain the second issue which relates to dialogue between companies and investors.

Please turn to page 28. In recent years, passive equity investment has become further prevailing. Because of this, the survey results confirmed that the number of investors who have undertaken collaborative engagement is increasing.

Moving onto the next page, which is page 29. During past discussions by the Council of Experts on the Stewardship Code, some points were made regarding institutional elements (the legal framework for collaborative engagement and so on) that support constructive dialogue. In particular, in relation to the large shareholding reporting system, some people have previously pointed out that the scope of such terms as "joint holder" and "act of making important suggestions" is unclear. In this regard, in 2014, the FSA published "Clarification of Legal Issues Related to the Development of Japan's Stewardship Code". However, even after that, as the FSA confirmed and wrote in the "Proposed Revisions to the Stewardship Code" published in December 2019, some still say that the scope of collaborative engagement is not clear.

Furthermore, as shown in the bar graph at the bottom, according to a survey conducted by the Japan Investment Advisers Association last year, we are aware that some asset managers still mention a “lack of clarify in the judgment criteria for ‘act of making important suggestions’” or a “lack of clarify in the judgment criteria for ‘joint holders’”.

I will skip the next page and move on to page 31. This is another topic, and it relates to an institutional issue. In recent years, while there has been an increase in shareholder proposals, listed companies have pointed out that, from the perspective of deepening dialogue with shareholders, a system to confirm substantial shareholders should be considered. As an example, this was pointed out in a report published in July 2020 by the Ministry of Economy, Trade and Industry’s Study Group on the Process of Shareholders Meeting in the New Era, as quoted at the bottom of the page.

That completes my explanation of the materials for today’s discussion. Finally, on pages 33 and 34, we have summarized the topics we would like you to discuss. The list is quite long, but I will read it out, nevertheless.

First, regarding “Interim review following the 2021 revision of the Corporate Governance Code”. Since the formulation of Japan’s Stewardship Code in 2014, a series of corporate governance reforms have been implemented. However, the number of empirical research studies on the effects of the reforms is not yet large, and the evaluation of their effects has yet to be determined. On the other hand, companies that have reformed their corporate governance system in an original and ingenious way have indicated that they are realizing certain effects, such as the enhanced deliberations at the board of directors. In light of this, how are you evaluating the effects of corporate governance reforms to date? What are the views of members on how the government should take into account the experience of companies about the effects of their corporate governance reforms and criticism of the reforms, such as that the Code should not be made into detailed rules? Other than the papers listed in this presentation, are there any analyses that should be looked at as part of the review? And, based on the evaluation, are there any issues that need to be addressed in future corporate governance reforms? Lastly, are there any corporate initiatives that should be discussed in detail at future meetings of the Council?

The next subject to be discussed is about challenges for sustainable growth. First of all, although corporate governance reforms have encouraged Japanese companies to make investment that would contribute to their sustainable growth (capital investment, R&D/intellectual property, human capital investment, etc.), these investments have grown only modestly compared to those in the United States, and therefore, retained earnings have accumulated, especially in the form of cash and deposits. Under such circumstances, while the importance of investment in intellectual property and human capital, which

are the basis of value creation, has been discussed by the government, etc., initiatives by companies have been sluggish so far.

In order to make effective use of retained earnings (especially cash and deposits) that continue to accumulate at Japanese companies, we would like you to share your views on the following points. The first point is about appropriate allocation of management resources (capital investment, R&D/intellectual property investment, human capital, etc.) to improve corporate value over the medium to long term, as well as the balance between growth investment and shareholder returns with consideration of cost of capital. The second point is about companies' policies of holding cash and cash equivalents under highly uncertain conditions, such as the COVID-19 pandemic, higher prices of natural resources, and the situation in Ukraine. The third point is about the roles of the board, shareholders, and dialogue between the two when tackling the above issues, and the nature of corporate accountability.

Finally, with regard to issues related to dialogue between companies and investors, while various discussions and investigations are making progress on ideal constructive dialogue between companies and investors, during previous meetings of the Follow-up Council and the Council of Experts on the Stewardship Code, members have pointed out the lack of clarity in the scope of collaborative engagement (or collaborative engagement). So firstly, do you think we should consider any responses to address the issues raised so far? Secondly, are there any other issues that should be considered in terms of institutional settings related to engagement?

That's all from me.

[Kanda, Chair] Thank you very much. Now, I would like to ask the representative of the Tokyo Stock Exchange to provide explanations. Mr. Ao, I'm handing it over to you.

[Ao, Senior Executive Officer, TSE] I'm Ao from the Tokyo Stock Exchange (TSE). I would like to report on responses of listed companies to the revised Code that the members discussed last year. While we are recognizing that the effectiveness of governance reforms is more important than formal measures, today I would like to introduce some objective data here. Since the numbers and ratios quoted in this material which presents a general overview of the situation do not necessarily directly indicate whether governance is essentially good or bad, please note that these are only for the reference purposes.

Page 1 of Material No. 3 provides an overview of the revisions. Today, I would like to explain the situation regarding the main revision items, which are indicated in bold letters.

On Page 2, you can see graphs showing percentages of companies which appointed independent directors in the Prime Market. These graphs indicate that appointment of independent directors continue to progress, and that the number of listed companies at which independent directors account for more than

one-third of the total have increased to more than 80% as of April. This increase can be attributed to the appointment of outside directors ahead of schedule, especially at companies whose fiscal year ends in December that have chosen to join the Prime Market. On the other hand, while the percentage of listed companies at which the majority of directors are independent directors has increased, it is still less than 10%. This data is collected before companies whose fiscal year ends in March hold general shareholder meetings in June, so we expect to have a clearer picture of the general trend after the closing of such meetings, and we will update you on the situation sometime in the summer.

The graphs on page 3 show changes in the number of the Prime Market-listed companies that have established a statutory or voluntary nomination committee and remuneration committee. These are also increasing. For both nomination committees and remuneration committees, the percentage has increased to about 80%. As with the appointment of independent directors I mentioned earlier, we would like to update this data again, as we are sure the situation will have changed after companies have held their shareholders' meetings.

Page 4 shows the status of disclosure of skills that the board should have. The percentage of companies that comply with this principle is about 70% as seen in the former TSE First Section, and 30% of the companies that choose to explain are also considering how to comply with this principle in preparation for their next AGM. As you may know, the key point here is character of candidates and or actual selection of directors, in any case progress is being made on the disclosure side. As for the most common method of disclosing the combination of necessary skills, as shown in the pie chart using data of TOPIX 100 companies, the so-called skills matrix is used in the majority of cases.

Page 5 is about the appointment of core human resources. The revised Code requires companies to set measurable goals for the promotion of women, foreign nationals, and mid-career hires to core positions. Looking at companies that were previously listed in the TSE First Section, about 70% of them are complying with this principle. On the other hand, some companies have not yet set targets for any of these three attributes even though they have reported that they comply with the principle. For example, as shown at the bottom of the page, when looking at TOPIX 100 companies, we see that there is a considerable difference in goal-setting for women, foreign nationals, and mid-career hires.

Page 6 describes the state of sustainability-related activities. First of all, we can see that more than 90% of the former TSE First Section-listed companies are recognizing that sustainability is an important management issue. On the other hand, when it comes to specific action such as formulation of basic policies and disclosure of relevant initiatives, the compliance rate is between 60% and 80%. We believe that this is an area where further improvement can be expected in the future. Looking at the TOPIX 100

companies that are disclosing information at this time, there are many examples of companies disclosing information on their own websites or in integrated reports. Looking at the status of disclosure based on the TCFD recommendations, which was recently incorporated in the Code as a principle for the Prime Market, as shown in the graph on the right, nearly 80% of the companies already had disclosures based on the TCFD recommendations, and I think it can be said that TOPIX 100 companies are taking the lead in such disclosure.

Skipping page 7 and going to page 8, this page shows the status of disclosure in the English language, which is incorporated in the Code as a principle for the Prime Market. As shown in the graph on the left, the number of the Prime Market-listed companies that are disclosing information in English is steadily increasing. The graph on the right shows the percentage of English disclosure by document type. Higher percentage of English disclosure was marked for earnings reports (i.e. *kessan tanshin*), IR presentation materials, and convening notices of general shareholder meetings including reference materials.

Page 9 summarizes implementation rates of English disclosure by market segment. Please refer to the tables later.

Please turn to page 10, which also shows the use of the electronic voting platform that has been incorporated in the Code as a principle for the Prime Market. Of the Prime Market-listed companies, over 90% are going to use this platform, increasing compared to last year.

That is the end of my explanation, sorry if it was a bit rushed. Thank you.

[Kanda, Chair] Thank you very much. We have received opinion statements from Ms. Waring and Mr. Toyama, who are absent today. I'd like the secretariat to share the summary of their statements.

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

So let me begin with a summary of the written opinion from the Ms. Waring. We have received a wide range of opinions from Ms. Waring on 10 areas for improvement, so I briefly discuss each item one at a time. The first point written on page 2 is about "the quantity of independent directors". Ms. Waring recommends that a timeframe should be set for raising the percentage of independent directors.

The next point is about "the quality of independent directors". Ms. Waring acknowledges that there are various opinions, and recommends enhanced disclosure that contributes to the evaluation of the quality of independent directors.

As shown at the bottom of the same page, the third point is about "diversity, equity, and inclusion". Ms. Waring recommends, for example, that companies demonstrate their commitment to board diversity, equity, and inclusion in clear policies expressing goals, action plans, and measurable, time-bound objectives.

The fourth point is about “committee adoption”. Here, Ms. Waring recommends that all Prime Market-listed companies adopt a three-committee system.

I’m moving onto the next point on “capital allocation”, which is a long large section spread over two pages. Ms. Waring recommends in the paragraphs starting from “Going forward, we recommend”, for example, improving disclosure around the rationale for capital allocation decisions, improving disclosure about the rationale for holding non-core assets, and enhancing disclosure about the cost of capital.

Regarding her sixth point, “cross shareholdings”, she has written various comments, for example, her opinion is to propose that more companies provide more information on the rationale for why they hold cross-shareholdings.

Then, on page 6, under “corporate governance disclosure,” in the middle, she recommends, for example, that AGM notices and the Securities Reports are published at least 30 days in advance of the AGM, and the companies make changes to allow AGMs to be held in July. Furthermore, with regard to materials, she recommends that companies provide English translations for both their Securities Reports and Notice of AGM.

Her eighth point is about “sustainability disclosure”. In the second paragraph on the next page, she recommends that sustainability information be disclosed more extensively in annual securities reports and other voluntary corporate disclosure materials.

Moving on to her ninth point, which is “collective engagement”, Ms. Waring expresses the opinion that it would be helpful for the FSA to publish guidance on engagement.

Next, the tenth point, which is her last point, is about “enhancing dialogue between companies and investors”. In a nutshell, Ms. Waring suggests that companies should try to improve dialogue through the “comply or explain” system.

That completes my explanation of Ms. Waring’s opinion.

Next, I would like to explain another opinion submitted by Mr. Toyama.

In the first section titled “Issues related to the substance and effectiveness of corporate governance reform,” Mr. Toyama asserts that the biggest challenge in realizing substantial governance reform is to ensure the quality of people who lead the reform, and refers to the quality of independent director and the quality of human resources on the management side as issues to be addressed. Then, in the next bullet point, he argues that, in order to “enhance” corporate value, and especially to promote growth in the era of disruptive innovation, the required level of quality of the management as well as quality of the governance function that selects and supervises the management is extremely high. He believes that the number of problem areas that can be resolved by further revisions and detailing of the Code is decreasing,

and more effort should be focused on other measures to improve the quality of leaders. As indicated in red font at the bottom, he suggests that we should establish a model outside director eligibility criteria as a best practice.

Mr. Toyama's second point relates to "challenges of governance reform to eliminate a tendency for underinvestment". According to Mr. Toyama, the root of the problem of retained cash and underinvestment in human resources lies in the fact that the industrial and business models of Japanese companies are in large part based on a mass-production and mass-sales model that relies on tangible capital investment, and such a model is outdated and fragile, having been left behind in the age of knowledge-intensive, disruptive innovation. The question should be set as to how to encourage high-risk future investments in an era that requires uncertain investments in discontinuous areas, such as exploration of new growth opportunities, innovation investments, and acquisitions to obtain new organizational capabilities needed to transform their business models. Mr. Toyama is of the opinion that the focus should be on what governance reform can accomplish in this regard.

Finally, his third point relates to "the positioning of the revision of the Stewardship Code". With regard to the Stewardship Code, Mr. Toyama does not recognize it as a major issue for the time being within the framework of the current new capitalism debate. Rather, he sees the challenge for institutional investors, in corporate governance, as being the risk of a decline in the quality and quantity of engagement leaders, and believes that this is an issue we should focus on.

That's all from me.

[Kanda, Chair] Thank you very much. I would now like to spend some time for the questions and discussions of the issues raised. The items to be discussed are listed on pages 33 and 34 of the secretariat's material [Material No. 2], so please refer to them as appropriate. However, you do not have to stick to these items. We would like to hear a wide range of opinions, since today is our first meeting of this fiscal year, or should I say, the first meeting after restarting the meetings.

As time is limited, as is always the case, we have to calculate the time to allow each of you to speak, for which I apologize in advance. I think each person should speak for no more than about five minutes. Please bear this in mind.

If you wish to speak, as usual, please write your name and indicate that you would like to speak in the chat box. I will keep my eye on the chat and call on you to speak. After I call on you, please unmute your microphone and speak, and when you have finished speaking, please set yourself to mute again.

So, if anyone would like to speak, about anything, I would appreciate it if you send a chat message. Who would like to speak?

Thank you. Mr. Oba, please go ahead.

[Oba, member] I am sorry, but I would like to be the first to speak because I have to leave early today for another engagement. There are so many points at issue that it is very difficult to choose which one to start with, but I would like to narrow down my comments to two points.

My first point is related to how we evaluate the current situation [of governance reforms], which is one of the topics up for discussion. Unfortunately, although some companies may have achieved great results in their individual businesses, when viewed as a whole, I do not think that we see much improvement in the effectiveness [of governance reforms].

The main reason for this would be that boards, or rather management teams, are not really focusing on current market valuations. As a recent example, President Nagamori of Nidec Corporation, who appeared in the news recently because he was reappointed CEO, stated that the main reason for his return was that he was not happy about the current market valuation [of Nidec]. It is very important that these matters be discussed at board meetings as well as by the management team, but it seems that such matters are not reported very often. I believe that this is the first issue that needs to be addressed. That is my first point.

Another point is the issue of the Code being too detailed, which also relates to the issue of how we should address the criticism that the Code should not be more detailed. As explained by Director Hirokawa, looking at the survey of companies, many responded that they are feeling a lot of pressure. A trend is being created in which companies must comply with the Code. While it may be very important to disclose compliance rates, I think the current evaluation, where an increase in compliance rates is interpreted as an improvement of corporate governance, is putting pressure on companies. In the first place, since the Code adopted a principle-based approach, I think we should return to basics where each company can develop and express its own creative approach to corporate governance taking into account the principles of the Code. Therefore, I believe it is essential to dispel the tendency to consider that it is desirable to “comply” with the Code.

That’s all for the two points I wanted to make.

[Kanda, Chair] Thank you very much. Anyone else?

Thank you. Mr. Sampei, please go ahead.

[Sampei, member] This is Sampei. I would also like to briefly state my views on issues 1 and 2.

First of all, regarding the interim review, if we go back to the purpose of Corporate Governance Code, what it says there is that, “the Code is formulated as part of Japan’s economic growth strategy” and that “its primary purpose is to support sustainable corporate growth and increase corporate value over the mid-

to long-term”. This means that what we should be doing in the interim review is verifying growth and increase in corporate value. It is extremely important to face the results head on.

It has been eight years since the two Codes were formulated, and eight years since the Ito Review indicated a minimum ROE of 8%, and seven years since the CG Code was introduced in 2015. So from the perspective of Japan’s typical three-year medium-term plan, two cycles have been completed. Therefore, I believe that sufficient time has passed for this kind of verification.

Regarding what points should be looked at during the verification, for example, changes in market capitalization, which is influenced by the external environment and other factors, may be measured on a scale relative to overseas markets. Furthermore, as Mr. Oba just mentioned, in terms of market evaluation, we should look at typical, easy-to-understand indicators such as PBR, as well as ROE and ROIC which are the basis for market evaluation, and, what the growth rate is like. As far as I can tell, it is hard to say whether progress has been made yet. After the completion of two medium-term management plan cycles, companies were supposed to secure a ROE that would exceed the cost of shareholders’ equity, then receive cash flow from the invested project that should have been returned, and move on to investing in growth. However, I think that companies have yet to turn the corner on growth.

Next, I agree with the point about the Code not being too detailed. The Code adopted a principle-based approach, and I suspect that it has not yet fully taken hold. Therefore, I do not think that we should move toward the idea of more detailed regulations without first ensuring the principle-based approach has taken root.

In terms of the analysis that should be looked at to examine reforms, the phrase “decisive decision-making” has been used many times when introducing the Code. I think what this is referring to is reforms of the business portfolio. We also need to look at whether or not this is happening.

In terms of the issues to be addressed in the future, I think “change” was the keyword in the previous revisions of the CG Code. Therefore, I think it is still important to ask questions such as whether companies have gained the ability to respond to changes and whether they have reformed their management.

Finally, with regard to something I would like to see covered by the Follow-up Council in the future, I am very concerned that despite the introduction of the two Codes as part of the growth strategy, the market does not actually expect that many Japanese companies to grow. Therefore, even if we get such companies to talk about their growth strategies, the market is not listening to them, and a large gap with the market is emerging. I think we need to carefully analyze the current situation and understand the problem with regard to this issue.

As for my second point, regarding the issues for sustainable growth, I think the important point is that when we refer to the appropriate allocation of management resources, we may be ignoring returning committed capital. Returning committed capital includes sale of and withdrawal from businesses. Of course, there is also returning committed capital due to success. Therefore, I think that growth investment and returning committed capital are equally important. As for the accumulation of retained earnings or cash and cash equivalents, if we look at the details, we see that companies do not have earning power, so they hoard retained earnings or cash and cash equivalents in order to play it safe. So it is my belief that earning power and balance sheet issues are two sides of the same coin.

And another point, collaborative engagement is mentioned as an issue related to dialogue between companies and investors, and the reason why we need to review it at this time is because of its difference from traditional “collective engagement” which mainly focus on joint proposal-like activities. On the other hand, what is now referred to as “collaborative engagement” is more like, for example, an environmental initiative, where investors first agree upon the direction and collaborate in such initiatives. And by doing so, when shareholder proposals, etc. are subsequently made, it would be strange not to get on board with such proposals, and although “getting caught up” may not be the right way to put it, they ultimately join in. I think in this case it is hard to tell whether they are joint holders. Therefore, even if each shareholder does not hold 5% of shares, if they become joint holders, they will be caught in the act of making an important suggestion, and will be involved in large shareholding reporting. Thus due to the need to sort out these issues, we are seeing new developments that were not in place a few years ago, which means that we should take another look at them.

While there are three requirements for the applicability of an act of making important suggestions, one of the key ways to distinguish the applicability of the “suggestion” is, in my opinion, whether or not it is coercion. Even if a suggestion is made, I think we should reexamine whether corporate management ultimately has room to make decisions, or room to make a choice, or whether it is something that is being coerced through the collective exercising of legal rights such as voting rights, for example.

Furthermore, in the interpretation by the FSA thus far, for example, it is stated that simply asking questions as part of their research activities is unlikely to fall under the category of the act of making important suggestion, or expressing one’s own opinion in response to an issuer’s request, or taking a passive act such as providing one’s opinion at a meeting that was set up voluntarily by the issuer does not fall under such a category. I think this is inconsistent with the interactive nature of dialogue. Therefore, I am concerned that unless we once again sort out the issue of deepening dialogue and whether it constitutes the act of making important suggestions, we will not be able to expect in-depth dialogue.

One other final point, relating to so-called engagement between companies and investors, I think it is naive to think that all investors can engage in the same way that contributes to increasing corporate value. Furthermore, I think it is important to remind institutional investors that when they are actually engaging, they should be bringing up issues that serve the interests of many other general shareholders. This relates to when I came into contact with the British style of engagement about 20 years ago, and also to my interaction with an American relational investor who encouraged active ownership. In both cases, I vividly recall them saying that, “The most important thing to keep in mind is not to impose only our own principles, but to think responsibly about whether such principles are aligned with the interests of other general shareholders”. I think we need to reaffirm this stance.

That’s all from me.

[Kanda, Chair] Thank you very much. So I have received a lot of chat messages. Thank you. I will ask you to speak in the order I received your chat messages, starting with Mr. Tsukuda.

[Tsukuda, member] This is Tsukuda. I would like to discuss the effects and the challenges of corporate governance reform.

First, I have two points about effectiveness. The first one is related to strengthening the functions of the board. By bringing an outside perspective to the board, in the form of independent directors, Japanese companies are beginning to recognize the most basic function of the board, which is the oversight of corporate management and the management team. I see this as being one of the major effects of governance reform.

Then, my second point is related to dialogue with institutional investors. I feel that we are making progress, albeit gradually, toward the major goal of making the investment chain function, which is also the purpose behind the introduction of both Codes.

So those are my two points on effect. But on the other hand, as governance reform progresses, the challenges are also becoming clearer. I’d like to briefly make three points about the challenges.

My first point relates to the cost-effectiveness of governance reform. In practice, some companies have been able to link governance reform to the improvement of their corporate value, while others have only superficially worked on reforms and have been unable to link reforms to the improvement of their corporate value. In the latter case, companies tend to criticize the detailed principles of the Code, and I understand that, but I think it is necessary to recognize that governance reform takes time, and that we need to be persistent in our efforts without rushing to conclusions. From that perspective, I think this interim review is an excellent initiative. I believe it is important to conduct this kind of verification at each milestone and to take a good hard look at the cost and the effect of reforms.

My second point relates to reaffirming the purposes of governance reform. In Japan, we talk about “growth-oriented governance reform”, but I think the important to note that governance reform is a means, not an end. I believe it is important to realize the offense or growth-oriented management and growth-oriented business execution by bringing an outside perspective to the board, supervising the management, and encouraging management reforms. I think the situation at Hitachi that Mr. Higashihara mentioned earlier is a best practice in this regard, as it produces offensive or growth-oriented managers and encourages decisive management decisions. I think it is essential to encourage Japanese companies to realize that decisive management decisions are important. Many Japanese companies still have a way to go in this regard.

Finally, my third point relates to concerns about short-termism. Although it is not the main point this time around, it may have some effect on collaborative engagement. I am a bit concerned about whether short-termism is rampant. Various shareholder proposals are being made, such as requests for shareholder returns. I sometimes come across cases that make me wonder if this is short-termism at play, or in other words, cases that make me question if it is really good from the viewpoint of the common interest of shareholders to return all future cash flow over the medium to long term to the shareholders now. Of course, shareholder rights are important, and I am sure that there are many excellent shareholder proposals, but I believe that it is important to improve corporate value over the medium- to long-term, and that we need to keep a look out for short termism.

That’s all from me.

[Kanda, Chair] Thank you very much. Next up is Mr. Obata, please go ahead.

[Obata, member] Thank you for the opportunity to speak. As a business person, I would like to make three comments.

First of all, regarding the interim review of Corporate Governance Code, I believe that companies are taking the Code seriously and responding to it. That said, I believe that governance adopted by companies is a part of their competitive strategies. With regard to the type of governance system adopted by companies, I believe that each company should decide what governance structure it will adopt in its own way, taking into account the environment and circumstances in which it operates, and of course, thoroughly understanding the Code. Based on this, since the current Governance Code contains quite detailed provisions, I believe that it would not be appropriate to revise the Code or make it any more detailed at this stage, but rather I think we should leave it as it is for the time being and let each company plan their own initiatives while keeping an eye on the Code itself.

My second comment relates to the positioning of outside directors. My view is that, based on the

results of a series of corporate governance reforms, what is being required of outside directors has changed considerably. In addition to the previous practice of having the outside directors attend board meetings to discuss issues, it is now necessary for them to commit a great deal of time to fulfill their roles. As for their attitudes toward a company where they serve as outside directors, I believe that it has become extremely important how to foster the desire to improve the company. Given this situation, as was mentioned earlier, I think it is necessary to further improve the quality of outside directors, and at the same time, I think there is a shortage of people willing to serve as outside directors. In this respect, in terms of how we can improve the actual governance aspect in the future, I think it is essential to increase the number and quality of people willing to take on the role of outside director and I would like us to discuss this in the future.

In addition, I think the key point will be how companies should provide necessary information to outside directors so that they can discuss the company's business strategy. If the number of matters for resolution is reduced, and reports are made on all kinds of topics, it will be very difficult to run board meetings within the constraints of the time allotted for such meetings, and this is something I am concerned about.

Finally, my third comment relates to something pointed out earlier about the identification of substantial shareholders. If substantial shareholders are made more visible, I think that they will become a factor for companies to take into consideration not only from the perspective of dialogue but also when considering the company's capital policy and so on. And so I would very much like to see various studies being conducted in a form that goes some way to identifying substantial shareholders.

That completes my three comments. Thank you.

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

[Kawakita, member] This is Kawakita. First, I think one problem is that there are still many companies with a PBR below 10%. About half of companies listed on the former TSE First Section or the Prime Markets have consistently recorded a PBR below 10%. There is a strong possibility that such companies, in short, are not valued by investors. From this perspective, since the introduction of the two Codes, their substantial effect has not yet been demonstrated. This suggests to me that there is a need to further improve the effectiveness of the Codes.

That said, I recognize that the two Codes have covered most of the areas that need to be defined. Of course, I am not denying that some parts need to be revised or that some additions are necessary, but it does mean that there is no great need to keep further enhancing the Codes.

I would like to raise three issues based on what I have just said, the first being the lack of engagement of asset owners and asset managers, in my opinion. This has been a particular concern of mine since

discussions relating to the Codes began. Passive management using TOPIX or even using TOPIX as a benchmark has become the mainstream. The number of investee companies has exceeded 2,000. This is an awfully high number. 2,000 is not a realistic number of companies that individual asset managers or asset owners can engage with or provide instructions for engagement. Therefore, I believe that we have reached the stage at which asset owners and asset managers should devise an index to be used passively or as a benchmark.

For example, TOPIX has various sub-indexes. Earlier today, TOPIX 100 was used by the TSE in their explanation. So, we are at the point where we need to consider what is appropriate, and especially what is an appropriate index for engagement.

The second issue is that I am very concerned about the one-size-fits-all approach to dividends: the notion that dividends should be paid, and the dividend payout ratio should be around 30%. Each company has different levels of business maturity and investment opportunities for growth, and the amount of retained earnings they require naturally varies accordingly. So, I believe that engagement with companies cover topics relating to retained earnings, not dividends. How much is needed as retained earnings? By determining the amount of retained earnings, you can then determine the amount of dividends from the remaining amount.

I think that this kind of engagement, from the investor side, will pave the way to solving the problem of excess cash and deposits, as outlined in the FSA's material [Material No. 2]. And, I think companies need to be proactive in providing investors with information concerning their need for retained earnings, growth strategies, and associated investment plans.

The third issue comes from a slightly different perspective, and relates to the quality of directors. There have been a noticeable number of cases in which outside directors serve concurrently on the boards of three or four companies. As a result, I think outside directors will inevitably end up providing a perfunctory discussion. In fact, I have heard from influential outside directors that it is already challenging to serve as an outside director at just one company, so how is it possible for one person to serve on the boards of three or four companies? I think this is one example of a loss of substance of the Code. When you allow one person to serve concurrently on the boards of several companies, it leads to merely formal compliance of the Code [in terms of principles on outside directors]. So in this sense, it is necessary for companies to recruit a wide range of human resources, and I think we have now reached the stage at which we should discuss how to expand the pool of human resources if there is a shortage of such human resources. I believe that asset owners and asset managers should bring up, during engagement, the issue of whether it is acceptable for one person to serve currently on the boards of three or four companies.

That's all from me.

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

[Okada, member] This is Okada.

Thank you for conducting interviews as part of the interim review. I appreciate the effective review. I'm sure there are many opinions, but I believe that the revised version of the Corporate Governance Code is nearly complete in terms of presenting principles. Some interviewees expressed their opinions that companies are carrying out superficial reforms, and that investors are also exercising their voting rights based on the merely formal judgment criteria. However, the results of the interviews indicate that each company is using their own creativity, and many companies are making progress in their reforms. The interviews may have been limited to 16 companies, but I thought I could visualize such companies. It may take some time before this will lead to an improvement in corporate value, but I think it is safe to say that it has had some positive effect. Therefore, it is my opinion that the Code does not need to be any more detailed than it is now.

Autonomous improvement efforts by companies are essential for future development. Empirical studies and investor reviews would be useful to achieve such efforts. I hope that best practices will spread through empirical studies in the future. Furthermore, I think it is also important for companies to not only say that they have complied, but also to provide information on their specific efforts to improve governance, so that engagement with investors will become more effective. I think it is best to work on the assumption that there is no such thing as a perfect governance system of a company.

While companies should definitely be making efforts, it is also desirable for investors to listen to explanations rather than make judgments based on formalities, and even if the companies comply, for example, ideally their stance should be to evaluate efforts to make further improvements over the medium- to long-term.

I have one issue of concern following my participation in the Follow-up Council to date. It is not a problem of the Code, but I would like to discuss the number of outside directors. We need to wait for empirical research to see whether corporate value increases as a result of an increase in outside directors. I think the presence of outside directors raises the awareness within a company, and investors may not highly value companies with few outside directors. However, I do not think this is a simple problem that can be resolved by the number of outside directors.

First, it is great that more than 80% of the companies have appointed more than one-third of outside directors, but what is the significance of one-third? It is better than having two, which is of course a good thing if it means more is better than less, but it is meaningless unless outside directors are in the majority.

If we are aware of the issue of whether internal decisions can be overturned, in principle outside directors should be in a majority, and this is the direction we should be aiming for. Therefore, I think it will make most sense if we can devise a structure in which outside directors will provide checks and balances.

I think the issue is that there may be a problem with Japan's organizational design system. First, while "Company with *Kansayaku* Board (i.e. Audit & Supervisory Board)" is a company that operates on the premise that directors execute business. When outside directors are added to the board, in terms of monitoring and supervision, we will see a situation in which directors are both supervising and being supervised at the same time. This limits the check functions of outside directors.

On the other hand, "Company with Three Committees (Nomination, Audit and Remuneration)" is designed in a way where the majority of the members of each committee are outside directors, and such committees have more power than the board. And I think this is another reason why not many companies have adopted this organizational form. Such problems exist. Meanwhile, I have heard some people say that "Companies with Supervisory Committee" are also experiencing challenges. Taking all of this into consideration, ideally, we should first address the issue of institutional design or organizational forms stipulated in the Companies Act. However, I am fully aware that this is not a matter that will proceed easily. In order to make Companies with Three Committees function properly, not only do we need to revise the Companies Act, but we also need the companies which adopted such an organizational form to be serious in their efforts to reform. In that sense, I would recommend that the Prime Market-listed companies be encouraged to transition to Companies with Three Committees as a future direction. I'm sure it is not going to be easy, but as a future direction, we should encourage the companies to transition to Companies with Three Committees.

Also, even in case of Companies with *Kansayaku* Board, it is possible to use the creativity so that outside directors can properly perform the check function. Speaking from my experience, if an outside director raises a question or objects at a board meeting, the company should be given another chance to explain the situation to the outside director; and if he or she is still not satisfied, the proposal should be sent back or even rejected. I think it is possible to devise ways to increase the effectiveness of substantive governance in which outside directors have limited authority, even at Companies with *Kansayaku* Board, by making the final decision unanimous, or coming up with some similar arrangement.

In this respect, there are some issues with the institutional setting, and in a sense, the best practices of each company will come to life. And so, I hope that in the future investors will look at how companies are using outside directors.

[Kanda, Chair] Thank you very much. Based on the order in which I received chat messages requesting

to speak, I would like to ask Professor Kansaku to speak next.

[Kansaku, member] This is Kansaku. Thank you for the opportunity to speak. I'd like to make three points.

The formulation of the Corporate Governance Code and the METI's initiatives for establishing various guidelines on governance and outside directors, etc., that support the Code, have brought about significant changes in the corporate governance of listed companies, such as the appointment of outside directors and the increase in the number of remuneration and nomination committees, etc., and I think the significance of the Corporate Governance Code was enormous in this respect alone. This is because I believe that only after such formal arrangements are in place, we will be able to have more serious discussions on the ultimate goal of governance reforms, namely the sustainable corporate growth.

Therefore, while companies are working on developing or improving their corporate governance systems in terms of forms, such efforts should lead to effective corporate governance. To this end, we need to conduct further reviews of the Code, and continue to examine relevant forms as well. I presume that boards will discuss not only their companies' management strategies and portfolio reviews, but also sustainability governance and the companies' purposes, which I think will become even more important in the future.

Personally, I am interested in the composition of the board, agenda setting for board meetings, how boards operate, including separating the board chair and CEO positions, and best practices for various committees, including nomination committees and remuneration committees, to further fulfill their roles.

Secondly, I think it would be desirable for institutional investors, who have a fiduciary duty to the investors that back them, to conduct appropriate stewardship activities and ensure that shareholders' intentions are properly reflected in the agenda and proposals at shareholders' meetings and in board discussions, through dialogue with the management. I believe that there is room to further improve the environment so that institutional investors, including so-called passive institutional investors, can conduct effective and efficient stewardship activities and engage in constructive dialogue with the management, including on topics such as board composition, business strategy, and especially the use of retained earnings, including human capital.

In order for passive institutional investors to engage effectively, I believe that there is a need to promote and share the same outlook on collaborative engagement. There should be common understanding of when to conduct collaborative engagement, and ideally, legal stability should be secured by clarifying the definition and scope of joint holders and acts of making important suggestions, since the lack of such clarity is considered to inhibit such engagement.

In the EU, for example, requirements regarding the scope of joint holders and acts of making important

suggestions are fairly limited, such as when there is an agreement on the exercising of voting rights, or when there is an intention to make continuous and decisive changes to the company's management policy. Furthermore, I understand that the requirements are stricter and more limited than under Japanese law, such as clarifying that individual joint acts do not fall under the category of acts of making important suggestions. Although this will ultimately require legislative intervention, it seems to me that the concepts of important suggestions and joint holders should be reviewed and clarified in the direction of limiting them.

Thirdly, on the other hand, given that passive institutional investors do not necessarily have an incentive to actively engage in stewardship activities, and given that there are hostile corporate acquirers who try to buy up as much as possible in secret, it would seem desirable for a company and other shareholders to know who the shareholders are a little earlier, so that the management can encourage institutional investors and others to take appropriate action and so that other shareholders can take more appropriate action.

The UK has adopted a structure for quickly and accurately learning who shareholders are through a system for reporting large volume holdings and a shareholder investigatory powers system. On the other hand, anti-takeover measures are prohibited in principle, thereby enabling and encouraging dialogue between shareholders and the management from an early stage. In contrast, the US system for reporting large volume holdings is more relaxed than that in the UK and even Japan, and while the tender offer system and proxy solicitation system are actively used, anti-takeover measures are permitted and a balance between offense and defense is maintained.

I feel that, following the implementation of the two Codes, practical issues relating to corporate governance in Japan have become clearer. I believe that some of these issues extend to the state of the legal system. For example, it seems to me that there are some issues that need to be considered legislatively, including the stance Japanese law should take on the system for reporting large volume holdings and the shareholder investigatory powers by a listed company, as well as a review of the concepts of joint holders and important suggestions, that I mentioned earlier.

When considering such issues, it seems to me that we have reached a stage in which we should consider a system for reporting large volume holdings and a shareholder investigatory powers system, including legislative discussions, taking into account the relationship with tender offer regulations and hostile anti-takeover measures, as well as the basic future state of corporate governance at listed companies in Japan.

That's all from me. Thank you very much.

[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 a number of opinions on the topics listed on page 33 [of Material No. 2].

First, regarding my thoughts on the effectiveness of corporate governance reforms, I believe they have been effective. Although it is difficult to obtain clear results in terms of macroeconomic figures, if you look at individual companies, you can see the nature of the board has changed dramatically. In my work, I have observed many corporate boards, and I have seen many situations in which boards have made changes through reforms, and as a result, the content of their discussions changed, and this was then reflected in the formulation of their mid- to long-term strategies. What these companies have in common is that, while their approach and their reforms varied, their intention was to enhance the board's oversight function. The notion that enhancing the board's oversight function is critical to increasing corporate value was shared by all the companies I looked at. The reason why such an important matter is shared, is because the Corporate Governance Code clearly indicates the ideal form of the board, and because various discussions on the Code have been conducted with this in mind, and because the content of these discussions is being shared by companies. I believe that this Follow-up Council is significant from that perspective.

And regarding the second topic concerning the Code's detailed regulations, I think that the Code itself should remain to be principle-based and details should be left to the discretion of companies. That said, it is certainly true that companies have a desire to know what they should do in concrete terms and what specific measures they should be taking. I think that examples from other countries can be helpful in finding a solution to this. In the UK, the Governance Code contains relatively simple principles, and at the same time that the code is revised, the authority publishes the guidance that contains more specific details for implementing the principles, including best practices. Companies can use the guidance as a reference for specific measures. We should probably consider such an approach for the next revision.

Next, regarding the timing of the revision, I think updating the Codes every three years, as is the case now, is appropriate. That is to say, the environment is changing rapidly, so even if the principles of the Code do not need to be changed much, I believe that a periodic review should be conducted. Even if, as a result, the content does not change much, I believe that verifying the revisions is, in itself, significant.

Next, finally, I would like to touch on future action. Development of various forms are currently underway. I am also of the believe that form is very important and that form dictates substance to a great extent. Since the development is well underway, I think that in the future, there will be heightened interest in the effectiveness in terms of substance as well as form. I think there are various points to be considered

regarding the effectiveness. For example, one of the points raised by Mr. Toyama and Ms. Waring related to improvements in the quality of independent directors. I feel that this is a very important point.

As to how to specifically improve the quality and competence of independent directors, as stated in the opinion submitted by Ms. Waring, I believe that conducting an evaluation of independent directors and individual directors as part of the board evaluation will be effective. In the Codes established by many major foreign countries, board evaluations tend to require evaluations of the board as a whole, committees, and individuals. On the other hand, the Japanese Code only requires an evaluation of the board as a whole, and evaluations of committees and individuals is only mentioned in the guidelines for dialogue between corporations and investors.

When revising the Code in the future, I think it would be good to discuss the details of the board evaluations, taking into account the global situation as well as the need to improve the competence of independent directors in Japan.

That's all from me.

[Kanda, Chair] Thank you very much. Going by the order from the chat, Ms. Matsuoka will be up next. Ms. Matsuoka wrote that she would like to speak once others have expressed their opinion and I think we have now heard quite a few opinions so I would like to ask Ms. Matsuoka to speak now.

[Matsuoka, member] Thank you. I am grateful to have the opportunity to speak.

Whilst I empathize greatly with the explanation given by Mr. Higashihara at the beginning of his self-introduction, for today's purposes, I would like to make my remarks mainly from the perspective of my role as the Chair of the Sub-Committee on Capital Markets of Keidanren (Japan Business Federation).

The Sub-Committee on Capital Markets of KEIDANREN has submitted its opinion in writing from the perspective of improving the effectiveness of the Code, which I would ask for you to refer for details, however allow me to take this opportunity to add a few comments.

First, regarding the issue of interim review of the revised Code, since Japan's Code is positioned as a growth strategy, the effects of the Code and corporate reforms based on the Code should be examined by evaluating whether the Code has led to enhancing corporate value on a medium - to long-term basis. However, given the recent economic situation, it may be difficult to fully recognize the result of increase in corporate value, or further time may be required. Going forward, we believe that further creative approach will be necessary to ensure that the efforts to meet the principles of the Code lead to sustainable growth. Ideally, we should continue to verify and confirm the significance, effectiveness, and challenges of each item in the Code.

Furthermore, certain issues have surfaced, such as investors not having enough time to hold sufficient

dialogues. While it is a given that corporations should endeavor to fully articulate and explain their direction and strategies, we also believe that shareholders, investors, and related parties should aim to improve the effectiveness of the Stewardship Code by enhancing corporate value through holding constructive dialogues with companies, instead of making judgements that are uniform or based on formality .

In addition, we feel that the government, companies, investors, and other market players should share the view that the Code is aiming for sustainable growth, and that “complying” and fully “explaining” are valued equally. For investors, we ask that they listen to the explanations given by companies, and make constructive suggestions and engage in constructive dialogues, in order to enhance the medium- and long-term value of companies that encompass a variety of stakeholders.

Next, on retained earnings and human resource investment, which are issues related to sustainable growth, we think it is necessary to look at retained earnings from the perspective of retained earnings ratios, and taking into account economic conditions and financial performance of corporates. Furthermore, amidst the increase in the lack of clarity and uncertainty in the business environment, due to the COVID-19 pandemic and geopolitical risks, a variety of risks must be considered and incorporated in corporate management. We believe it is necessary to carefully look at the support structure for companies, for example, the means of financing, taking into account the availability of options including direct financing, as well as the fact that retained earnings are used to assess company credits, and the reality of corporate revitalizations and M&A.

It is important for corporates to invest in growth areas and develop new businesses over the medium- to long-term, make capital investments, invest in R&D and intellectual properties, as well as in human capital; whilst maintaining a healthy and stable corporate condition. However, we think that each company is required to determine and explain whether and how these measures will contribute to their growth, in light of their business environment and management strategies.

Finally, regarding the issue of dialogue between companies and investors, we hope that clarifying the definition of joint holders and actions of significant proposals in conducting collaborative engagement will increase transparency in the market and promote constructive dialogues between investors and issuers. However, as this is a difficult issue that has been debated for many years, it would be meaningful to have thorough discussions at the appropriate forum, taking into account the opinions of both issuing companies and investors.

That’s all from me. Thank you.

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

[Katayama, member] This is Katayama from the Japanese Trade Union Confederation. Thank you for giving me the opportunity to speak. I would like to make two points.

First, I believe that the examination of the effects and impacts of corporate governance reforms is very meaningful in considering the future state of corporate governance. However, verifications focus on the performance of the company and its evaluation by the market, and I believe that whether the compliance system has been properly strengthened is also important in corporate governance, and that this will need to be verified in the future.

Second, I would like to point out that corporate investment in human resources is still inadequate. As stated on page 24 of the secretariat's materials [Material No. 2], I think the fact that companies' awareness of human investment is lower compared to that of investors is a major problem. I believe that we need to push from the perspective of corporate governance to build a management strategy to increase investment in human resources, through discussions with labor unions, discussions on medium- to long-term investment and financial strategies at board meetings, and constructive dialogue with investors.

That's all from me. Thank you.

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

[Ueda, member] This is Ueda. Thank you for the opportunity to speak. I found the report on the interviews conducted with companies in connection with the restarting of the Follow-up Council, to be very informative and I believe they will lead to more dynamic discussions. Thank you.

First, I believe that the revisions to the Code have been effective. By which I mean, that corporate governance, which I have been studying since I was a student, used to be a rather niche topic until about 10 years ago. It was something that only a few people were interested in, but now, no matter who you talk to, corporate governance is acknowledged as a serious issue, and I believe that this is a significant improvement.

However, in terms of the effectiveness, I sense that there is considerable polarization. This also relates to the next issue. In other words, there are two types of companies. There are companies that are serious about making improvements, want to make changes and feel they must make changes; and there are companies that are passively complying, based on the notion that they have to comply with the Code because it has been established. Herein lies the polarization.

It is important to note that the Code is principles-based and that the Code is not a law, but that while we want companies to adhere to the framework, we want companies to think about the substance of the framework, including what the substance might be. I wonder if we need to further increase awareness of the fact that the purpose of the Code is not compliance, but making improvements.

As for criticism of the detailed regulations, for example, the governance code in the UK is quite detailed, and even includes issue relating to workers. On the other hand, regarding the board structure, for example they are separately spinning out the Code, issuing guidance and guidelines that are really too detailed, as attachments. Such structures exist, and if, going forward, there are concerns about too detailed regulations, it may be necessary to consider such a structure in the future.

Then again, there are some principles which companies should comply with, specifically, the principle on disclosure, especially the issue of disclosure in the English language. The TSE did a really good job in their research, which was very helpful. For example, in order to increase the attractiveness and value of the Prime Market in the future, I think it is necessary to disclose English documents, including securities reports and convening notices together with reference documents. I feel that we need a system for sharing the view on “must have” and “nice to have”.

Regarding the next topic about the issues that should be taken up in the future, I will save that to the end. My next comment is about retained earnings, and it also relates to the current bipolarization. Companies that are exposed to the market are confronted by investors with a need for growth and so they seriously consider the idea of investment for this purpose. On the other hand, if that is not the case, as now, retained earnings may build up as a defense, for example, because of the situation in Ukraine, and this may not lead to investment for growth. This also relates to the Governance Code, and medium- and long-term corporate value, and for this reason, I think it will be necessary to organize them by dividing them to some extent on a time axis. For example, what about investment for growth in the short term, how retained earnings should be, and in the medium to long term? For example, I think that in the short-term companies will naturally respond to an emergency situation such as Ukraine. In the mid- to long-term, I think the focus will be more on R&D, intellectual property, or sustainability, and human investment from a more mid- to long-term perspective. I think that such classification will be necessary in the future.

My last point relates to dialogue, I believe that companies feel most strongly that investors are not uniform, as I think Mr. Sampei pointed out earlier. There have been some comments along the lines that investors have not approached companies in the first place. In addition to investors who look at corporate value, as passive investors increase, more investors will not look at corporate value and be only aware of it when they exercise their voting rights. Furthermore, as there are companies that are not expected to grow, or are judged to have no growth, such that investors do not ask for dialogue in the first place, I feel that this is not just about the Corporate Governance Code or the Stewardship Code.

So, as for the topics that I would like us to discuss in the future, the first topic that I would appreciate us discussing at a Follow-up Council meeting is, if the purpose of this year’s meetings is really to be a

follow-up rather than a near-future revision of the Code, then I would like to discuss topics that fall between the Code for companies and the Code for investors. For example, the issue of the quality dialogue, and the issue of cross-shareholdings, which may be relevant to both Codes depending on whether you are looking from the cross-holding shareholders side or the side whose shares are being cross-held. The second topic concerns the entire investment chain. More specifically, enhanced disclosure. What disclosure is necessary? I think it is necessary to increase transparency not only on the corporate side but also on the investor side. Then there is the importance of audits. In particular, as non-financial information and sustainability activities become more animated in the future, the quality of audit firms will be an issue as there is an increase in the number of small and medium-sized audit firms among listed companies' auditing firms. Since audit firms are also subject to the Governance Code, I would appreciate the chance to discuss the investment chain as a whole, which is something we usually cannot discuss when we focus on Code revisions.

That's all from me. Thank you.

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

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

Today's topic is the interim review following the latest revision of the Corporate Governance Code, and I would like to start by saying that, as has already been mentioned, I believe that the effectiveness of the Code has been positive.

On top of that, I would like to make three comments regarding the interim review, which means the interim review of this Follow-up Council itself, from the viewpoint of what we should focus on and follow up on to contribute to the original purposes of this Council, that is to deepen the transition from form to substance.

First, in relation to the Corporate Governance Code, as is mentioned in the points raised by the companies on page 3 of today's secretariat materials [Material No. 2], and as other members have also pointed out, I would not go so far as to say that companies are compliant supremacists, but I think it is true that companies are unable to fully break free from the principle of compliance prioritization.

In fact, it was in 2015 when this Follow-up Council was first established and issued its first opinion, and since then, in our opinions, we have continued to point out that there are many cases in which it would be of more value to actively explain the reasons for non-compliance rather than to just comply as a formality, and so we have been emphasizing the importance of explaining. But yet, this was once again pointed out today.

I think we have made various efforts along the way, such as changing the term to 'comply and explain'

instead of ‘comply or explain’, but we have not been able to get away from the notion that compliance comes first, because compliance reduces the burden of accountability.

I apologize for using this as an example, and I don’t mean to imply that the materials are bad or anything, but even in today’s presentation by the TSE, the compliance rates drew our attention as they are easy to understand. Then, based on an increase in the compliance rates, it is concluded that there has been a progress in governance reforms. Precisely because the compliance rates are disclosed, people are focusing on these rates. When this Follow-up Council considers that explanations are important, then we should forget about the compliance rate, which has been increasing to some extent, and our discussions should focus on the explanation rates, regardless of whether companies choose to comply or not.

Since an increase in the explanation rate essentially means an enhancement of corporate accountability, I think it would be a good idea to prioritize providing explanations first, and then proceed with the approach of leaving verifications of the details relating to the explanation to dialogue with institutional investors.

Next, moving onto institutional investors, regarding the issue that was pointed out today regarding the scope of collaborative engagement being unclear, and as one member pointed out, this is an issue that needs to be addressed from the perspective of transparency. However, from the perspective of the idea of “from form to substance,” which is put forward by the Follow-up Council, as some of the members pointed out today, this has already been clarified in other countries, and I was interested to hear what kind of suggestions and evidence of effectiveness have been provided for collaborative engagement in empirical studies overseas. In short, I think we need to clarify what is expected from collaborative engagement and why collaborative engagement takes place, based on precedents from other countries.

I read an article in the Nikkei Shimbun on the 22nd of last month that the FSA is going to supervise so-called greenwashing and ESG-washing of asset management companies without any substance. I think this may be related to today’s discussion about engagement. I think this is an area that can be monitored by the FSA to make sure that engagement, whether it’s individual or collaborative, is not just superficial or “engagement washing”, so I would like to see efforts being made from the viewpoint of deepening from form to substance.

Thirdly, the common objective of both Codes was always, from the time they were formulated, to enhance corporate value over the medium to long term, but as was pointed out in the secretariat’s presentation today, compared to overseas companies, there is inadequate investment in growth and shareholder returns at Japanese companies which has resulted in a buildup of retained earnings and cash and deposits. All of these factors contribute to the percentage of companies with PBR below 1, which is

significantly higher than that of overseas companies.

As Mr. Kawakita mentioned earlier, and as I read in the analysis he wrote in the Weekly Economist in December last year, even at the end of September last year, when the market environment was relatively favorable, as he pointed out earlier, 46.9% or almost half of the TSE First Section-listed companies have a PBR below 1, in other words, less than the dissolution value. From an investor's standpoint, if investment in business exceeds the cost of capital over the medium- to long-term, the company should invest in the business, otherwise it should be returned to the market, thus a PBR of less than 1, or so-called "dissolution value loss," is usually avoided, and so my understanding is that in the first place, there is a lack of awareness of the cost of capital. According to materials presented at the Follow-up Council meeting two years ago, on October 20, 2020, at that time, about half of the companies had not yet calculated their cost of capital. So, my final comment is that I think that one of the objectives of this Follow-up Council should be to increase the ratio of cost of capital management, so to speak, with the promotion of cost of capital management as a central part of the engagement agenda, in order to ensure that awareness of cost of capital takes root in Japanese companies. I am concerned about the current situation as there is no sense of crisis or rather a sense of crisis is not being fostered with regard to a PBR of below 1.

That is all I have to say. Thank you.

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

[Iwama, member] Thank you. I first got involved in this issue in 2013, when the Expert Group on Revitalization of Capital and Securities Markets was established, and at that time our discussions started with a debate on whether to introduce the Stewardship Code. I think we can all agree that a lot of progress has been made since then and that we are heading in the right direction.

In the context of what was happening at that time, it was very important to revitalize the capital market and the securities market, and the issue we focused on was the idea that if long-term investors make medium- to long-term investments based on sound knowledge, the investment will effectively function to increase the medium- to long-term value of the company. In which case, since passive investment has been increasing, it should be passive investors who need to engage with companies.

I am also an advisor to Norway's Sovereign Wealth Fund, which is a huge institutional investor that invests in listed companies all over the world. This fund is, put another way, buying up the market, so it actively engages with individual investee companies from the perspective that it is necessary to increase the medium- to long-term value of each portfolio company in order to increase the value of the portfolio. I am now involved with both the issuer side and the investor side. In case of an institutional investor, for

example, an investment advisory firm, its client is the asset owners and it works for the asset owners. And there are many cases where such asset owners are long-term institutional investors. What kind of feelings and policies they have on these issues is also a huge issue in itself? As Ms. Ueda pointed out earlier, I think it would be a good idea to take up the notion that problems that fall between the Corporate Governance Code and the Stewardship Code may lead to the revitalization of the investment chain as a whole.

I also think that one of the keys for such medium- to long-term investors to be effective in their activities is to have effective collaborative engagement, and I think that an environment needs to be created for that. This is not my area of expertise, but I think we also need to consider developing the legal environment.

Then, with regard to how boards have been working, I would say that, based on my very limited experience, this has changed a great deal. So, the issue now is exactly how seriously boards and committees are about increasing their effectiveness, and that's where the challenge lies. Conversely, I think it is also necessary for the engagement side to look at these things carefully before engaging in dialogue.

Also, the issue of retained earnings was raised earlier, and I think that from both the corporate and investor's perspectives, this comes down to whether capital is being used effectively. As has been pointed out by quite a few members, I wonder how conscious people are of the cost of capital, and whether it all measures up to the cost of capital. I think this should also be required to be used as a focal point for engagement.

My comments were a bit all over the place, but that's all from me. Thank you.

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

[Okina, member] Regarding the effectiveness of the Code, it was introduced in 2015, and I think corporate value has improved to a certain extent, but as many others have mentioned, the problem of there being many companies with PBR below 1 has always existed, and I think awareness of the concept of raising the return on capital above the cost of capital in the long term, as has been pointed out, has not yet taken root.

Next, I also share everyone's concern that, as mentioned today, instead of providing guidelines, the Code stipulates a set of numerical values, and therefore, companies tend to respond to the Code by superficially complying with such values. The market is inherently diverse in its perspectives, and I think we need to investigate changes in trends, such as the extent to which institutional investors are influenced by the advice given to investors by proxy advisors and the like.

For example, advice from proxy advisors on ensuring diversity can indirectly help drive corporate reform, but there is also the problem that proxy advisors are oligopolistic, and so it may be difficult to say that more explanation should be given for non-compliance amidst such a market structure. And this is something that I think it would be good for us to look into.

At the very least, it is very important to ensure the diversity of companies by improving their own governance in a way that suits their respective business models, while referring to the Code, explaining in some cases, and complying in others. That is one of my impressions.

Recently, economic security issues have become very big issues, and the yen has been weakening rapidly. This means that Japanese stocks are very attractive from a foreign perspective. While this is a good thing, from the perspective of economic security, for example, although various measures have been taken in the past regarding cross-shareholdings, I feel that we have now reached the point where it is necessary to consider various changes in the environment and to discuss them.

Next, regarding the issue of future corporate growth, as everyone has pointed out, it is very important for Japanese companies to sustainably increase their corporate value, and I too believe that investment in human resources is important. Today, someone mentioned the quality of the management and the quality of outside directors, and I think it is extremely important to train more and more people who are capable of taking on leadership positions such as CEOs and presidents in particular.

Investment in intangible assets, and I'm including investment in human resources in this, is very low compared to other countries, and we already wrote this into the Code in the last revision. Investment in human capital, as well as investment in intellectual property, data, software and so on, is low, and I think that it is important to properly tackle this issue.

These issue has already been written into the previous revision of the Code, and although the effects of this revision will not be seen until sometime in the mid- to long-term future, it will continue to be an important issue. I think we will see various guidelines being written about disclosure too, and I believe that it is important to continue to work on these issues.

In any case, although the Corporate Governance Code initially focused on shareholders, I believe that it is gradually becoming important to consider the interests of multiple stakeholders, in a medium- to long-term sense too.

Lastly, I have heard many comments about the importance of steady engagement by asset owners, who are responsible for engagement, and I also share this opinion. For example, I believe it is important for corporate pension funds, as asset owners, to fulfill a more robust role. Many corporate pension funds are committed to the Stewardship Code, but only three Japanese corporate pension funds have committed to

the UN's PRI principles. There is a little bit written about corporate pension funds in the Code. I think it is important to consider ways for corporate pension funds to contribute to sustainability, and I am personally aware that it will be a problem if these points cannot be written into the Code.

[Kanda, Chair] Thank you very much. I see that you have raised your hand. Mr. Takei, please go ahead.

[Takei, member] This is Takei. I have several points I want to make.

First, as everyone has pointed out today, there is a formalistic tendency to comply rather than to explain, and I believe that this is not only a problem on the corporate side, but there is also the problem on the institutional investors' side as well, including in the context of the vote exercise. The issue of how to improve the formal response on the institutional investors' side remains a challenge, nothing has changed, and this is something I think we should tackle properly.

My second point relates to the results achieved by Japanese companies as a whole. In Europe and the US, I think that measures related to this type of code are generally seen at a few hundred listed companies. In Japan, we may seek for another ways to look at the similar number of listed companies in Japan, such as the JPX400 or the TOPIX500. That is my second point.

My third point concerns the lack of investment in R&D, intellectual property, and human capital, as shown on page 34 of the materials. This issue was greatly incorporated into last year's revision of the Governance Code, and I believe that this is quite important, and that there is still considerable room for progress at Japanese listed companies in this area. Regarding this issue, for example, the Cabinet Office published Intellectual Property and Intangible Assets Governance Guidelines in January of this year, as stated in the materials. It stipulates that investment should be considered an asset not a cost, and it also says that investment should be linked to the business model, and that it should be explained using proper logic. I think that it is extremely important to properly tackle such issues.

Especially as the effects of human capital costs and R&D costs are never buried in a single year. Yet, despite this, for accounting purposes, companies can only take it as a single-year cost in the form of labor costs or R&D costs. As a result, there is a vicious cycle of targeting cost reductions when trying to raise operating income. In a sense, the management is being dragged down by accounting figures. I think it will be difficult or meaningless for Japan alone to change the accounting principles, so Japanese public companies should add back human capital costs and research and development costs that have a delayed investment effect to operating income, and add them back in the form of investments that will generate corporate value in the future, and then disclose and explain such calculations. I think it is very important to communicate these things to medium- and long-term institutional investors, both in Japan and overseas.

It goes without saying that, as a precondition for this, it is essential that these human capital and R&D costs have a meaningful impact on corporate value. Companies should use proper logic to explain whether the investment is linked to the company's purpose or its business model, and how it is connected to that purpose or business model, rather than simply increasing human capital costs or R&D costs. Moreover, such logic should also be used in dialogue with institutional investors. I think that, going forward, it will be very important for listed companies in Japan to visualize their human capital and intangible assets, and to visualize their value in this way and that there is considerable room for progress in this regard.

Also, in this kind of logical sequence, I believe that the current growing interest in sustainability is also relevant. Naturally this is limited to sustainability issues that have materiality relevant to one's own company. Before using the English word "sustainability," from a Japanese language perspective, working on behalf of the public raises the motivation of working people and human capital, it also increases their skills, and it adds value to human resources. This in turn lowers recruitment costs and training costs, and increases the utilization rate of various facilities. Since various positive logical flows can occur, one example would be to visualize the situation numerically, as being numerically positive in terms of corporate value. In any case, in this area of human capital, I think it is very important to be proactive. Looking to empirical studies published in recent years, for example, there are empirical studies that show that at a significant number of Japanese companies in the TOPIX 500 or so, there is a considerable positive correlation between labor and R&D costs and the improvement in PBR, which several people have mentioned over a 5 or 10 year period. As the Follow-up Council, I think it is extremely important for Japanese listed companies to work on this point, based on the revisions to the Governance Code last year. That was my third point.

Also, the last part of the materials refers to legislative issues. In this context I think this is referred to the large volume holding system, and I would like to comment on this point. The current large volume holding reporting system has been in place for about 15 years, since the last revision. During this time, as a number of people have mentioned, I believe that a considerable number of issues have built up that need to be addressed systematically from the perspective of transparency in the capital market.

In Europe and the US, various revisions have been made recently to increase transparency, and the issues of disclosure related to derivatives and strengthening enforcement have also come up. There is also the issue of understanding the substantial shareholders as shown on page 31 of the materials. Perhaps the issue of national economic security mentioned earlier by Ms. Okina may also be involved in some way. In any case, I think that making improvements in transparency in the capital market, including the large volume holdings reporting system, is a very important issue, and I think that the time has come to have a

proper discussion on the institutional response to this issue.

That's all from me.

[Kanda, Chair] Thank you very much. We have now heard from everyone who is present today. Chairman Higashihara made some comments in his opening remarks, but if you have any additional comments, we would like to hear them.

[Higashihara, member] This is Higashihara. Listening to everyone's comments has been very helpful, and has given me a good understanding of what has happened so far.

A number of points came to mind and I'd like to talk about them, and give you my personal opinion too. First of all, I got an impression that the Stewardship Code and the Corporate Governance Code have been quite widely adopted by companies over the past few years. And, although a number of opinions have been put forward about having more detailed regulations in the Code, my basic stance is that each company should be responsible for their own corporate governance. So the rules should be kept to the bare minimum, and if I may be so bold, what the corporate side wants is guidelines that show the direction, but if the rules are set in stone, I think that there is potential at Japanese companies today to make the rules a mere formality. So I would like us to consider that the initiative lies with the corporate side.

Next, I believe that the viewpoint of the president or CEO is particularly important. It is very important what kind of vision the president or CEO has with regard to the management of the company. It is important to share this viewpoint during discussions within the board of directors, and once a vision has been put together to a certain extent based on such discussions, the major mission of the president or CEO is to explain it to investors, and then to employees and the unions.

So, as was mentioned earlier in regards to surplus funds, I think it depends on the field and the current situation. The current situation being COVID-19 and war in the Ukraine. Surplus funds also depends on the business field being dealt with, so I think it makes sense for the president or CEO to think about such matters and then discuss them with the board. When thinking about the direction to take, I think it is important for there to be trust with the market. I think it is up to companies to improve the accuracy of the information they disclose, in terms of what information can be used in the disclosure, based, as much as possible, on the thinking of the board, president, or CEO. I think it is up to each company to decide whether surplus funds are needed, for example, whether it is time to focus on cash flow or cash, or whether it is time to retain this much money, including commitment lines, because of this or that risk, or whether it is time for investment in growth.

Next, regarding WACC, which was mentioned earlier, I believe that it is up to individual companies to determine how they view the details on their balance sheet. Whether it is done with ROIC spread or

various other things, is a matter for the companies to decide. How a company divides up its balance sheet into units, how it manages its ROIC spread, and how it looks at cash flow management is part of the operation of the company, and how it discloses this information to the market is an issue for the company to decide.

In contrast, for the past eight years or so, representatives of Hitachi have visited investors in the spring and autumn, engaging in actual discussions with major investors, listening to what they actually want, and making use of these discussions in our management. My feeling is that that Japanese companies will change considerably if they continue to promote such activities in the future.

That said, from here on in, as was mentioned earlier, it is important to practice sustainable management that includes environmental issues. And then there is also the issue of economic security that I mentioned earlier. And so, my opinion is that I would like the FSA and others to issue guidelines that say that this or that is the direction governance should take, and to create an environment in which companies can take the lead in governance matters.

That's all from me.

[Kanda, Chair] Thank you very much.

If anyone else would like to make any additional comments, please go ahead, as we would like to hear them. I take it that there are no additional comments?

In that case, we are slightly ahead of schedule, but I would like to leave it here for today. Thank you very much for many valuable comments and inputs you provided us today. If you have any additional comments or suggestions, please send them to the secretariat by email or some other means. I would appreciate it if the secretariat could sort through today's discussion.

Lastly, I'd like to ask the Secretariat if there are any announcements.

[Hirokawa, Director of the Corporate Accounting and Disclosure Division]

Regarding the date of the next meeting of the Follow-up Council, we will consult with the chair and make a decision on how to proceed from here and so I would appreciate it if you could wait for our announcement.

That's all from me.

[Kanda, Chair] Thank you very much.

I hereby declare today's meeting adjourned. Thank you very much for your active participation over such a long period of time.

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