

## **Responses to the Corporate Governance Code and Next Steps of the “Council of Experts Concerning the Follow-Up of Japan’s Stewardship Code and Japan’s Corporate Governance Code”**

### **I. Companies’ Responses to the Corporate Governance Code**

#### ***High Rate of Compliance***

Since the Corporate Governance Code entered into force in June this year, more and more listed companies are now submitting Corporate Governance Reports. So far, we find a high rate of compliance, an increased number of independent directors, and progress in disclosure of companies’ policies on cross-shareholdings.

In this Follow-Up Council, we need to examine whether these findings, including the high rate of compliance, are accompanied by substance. We also expect that companies and investors will constructively discuss these issues in depth in the process of their on-going dialogues.

#### ***More Explanation***

With regard to the Corporate Governance Reports which have been submitted so far, some members point out that there seems to be a tendency for companies to hesitate to “explain”, taking it for granted that “compliance” is necessary. At the same time, many members point out that we are encountering cases where companies proactively explain the reason why they do not comply with a certain principle and that these kinds of explanatory efforts are preferable to superficial compliance. However, it has also been pointed out that few companies give in-depth explanations: for instance, that non-compliance, rather than compliance, will lead to an increase in corporate value of that particular company.

There are also examples where a company specifically explains how to comply with a certain principle. Some members point out that other companies should make reference to such examples, because such effort contributes to constructive dialogues between companies and investors.

The Council expects that all Japanese companies will further enhance their explanations to investors, taking the above issues into account.

### **II. Next Steps of the Follow-Up Council**

We will hold a meeting every month for the time being, and discuss specific topics from the viewpoints of whether the form of enhanced governance structure is accompanied by substance,

whether enhancing governance will lead to a virtuous economic cycle over the mid- to long-term, and whether companies and investors are engaging in dialogue in a constructive manner.

We will publish statements on a regular basis each time we encounter tendencies which we believe we should call public attention to or examples which can be regarded as best practice.

The Follow-Up Council invites public comments on issues to be discussed and reviewed in its meetings, as well on further improvements of Japanese corporate governance. Please send your comments to the secretariat. For further details, please see our website below.

<http://www.fsa.go.jp/en/news/2015/20150924-1.html>

We will continue our discussion on the issues below that were raised in our first meeting on September 24.

#### (i) The Role of the Board

In order to declare that the board of a company is truly achieving “an independent and objective standpoint” as stated in Principle 4.3 of the Corporate Governance Code, appointing independent directors is not enough. The board is also expected to seriously review the company’s whole governance structure, including the separation of supervision and enforcement and the potential restructuring of the overall governance based on the results of the review. To what extent are Japanese companies currently taking on this kind of review process?

#### (ii) The Appointment and Dismissal of Top Management

When considering corporate governance, the appointment and dismissal of top management is extremely important. How should companies develop a succession plan? And how should they carry out the appointment and dismissal of top management based on the succession plan?

#### (iii) Cross-Shareholdings

While the level of cross-shareholdings is historically low compared to its peak level in the beginning of the 1990s, it is still at a certain level. While some financial institutions have already disclosed their policies on cross-shareholdings, we may need to review the overall situation, including the shift in the level of cross-shareholdings and actions by non-financial companies.

#### (iv) Dialogue between Companies and Institutional Investors

Although institutional investors are expected to engage in high-quality dialogues with companies to support the “awareness” of corporate managers, domestic investors do not seem to have reached that level yet. Also, the institutional investment role of asset owners in entrusting their assets to asset managers is important. Finally, we may need to review proxy advisors’ recommendations and how to use their services.