



**ICGN**

International Corporate Governance Network

## **The Council of Experts for the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code**

08 March 2018

Dear Fellow Council Members,

### **ICGN Response to Draft Guidelines for Investor and Company Engagement**

On behalf of the ICGN, I am pleased to submit our comment on the second Draft of the Guidelines for Investor and Company Engagement. This follows previous ICGN commentary provided on the 14<sup>th</sup> February.

We once again applaud the FSA and the Council for the efforts being undertaken to promote long term corporate value and sustainable economic growth. The development of this guidance can contribute to this objective by helping to enhance dialogue between companies and investors on issues of particular relevance in today's business environment in Japan.

ICGN approves the 'Guidelines for Investor and Company Engagement' as they are currently presented, notwithstanding that we respectfully suggest a number of further recommendations to be taken into account in the future as outlined in this letter. It is also assumed that ICGN recommendations will be considered as part of the review of Japan's Corporate Governance Code.

### **Context of the Guidelines**

As noted in previous correspondence, it is important to clearly state the purpose of the Guidelines which is understood to be a non-mandatory tool to help facilitate dialogue between companies and investors on issues which may be of particular current concern.

It is further understood that companies and investors are expected to embrace the spirit of the Guidelines which should be taken into account and this may be disclosed as part of their respective application of the Corporate Governance Code or Investor Stewardship Code. Some suggested amendments to the introduction of the Guidelines are therefore provided for your consideration to clarify these points.

### **Content of the Guidelines**

It is noted that a number of recommendations put forward by ICGN have been taken into account in the latest revised draft. The following further recommendations are suggested for consideration:

#### Guidance 3.2

ICGN welcomes reference to the role of a Nomination Committee to be actively involved in the appointment of the CEO. ICGN advocates that boards in Japan

should currently have a minimum of three independent directors and strive towards one-third of the whole board in due course. It should be noted that the ICGN preference in widely held companies is for there to be a majority of independent directors on the board.

We recommend adding reference to the Nomination Committee Terms of Reference in the Guidance. For example, *“Is the Terms of Reference for the Nomination Committee disclosed describing responsibilities such as: regularly assess the composition of the board taking into account the Diversity Policy; develop a skills matrix describing desired board composition aligned with the company’s strategic objectives; lead the process for nominating board candidates for shareholder approval; ensure that conflicts of interest among committee members are identified and avoided; oversee the process for board evaluation including the appointment of any external consultant, enter into dialogue with shareholders regarding board nominations; and lead the development, implementation and review of succession planning.”*

It is also noted that the Guidance could include reference to CEO succession plans being regularly reviewed and the importance of independent oversight should be emphasised in terms of CEO appointment and dismissal procedures.

#### Guidance 3.5

ICGN welcomes reference to the importance of an independent Remuneration Committee. We recommend adding reference to the Remuneration Committee Terms of Reference in the Guidance. For example *“Is the Terms of Reference of the Remuneration Committee disclosed describing responsibilities such as: determining the company’s remuneration policy; designing implementing monitoring and evaluating short-term and long-term incentives for the CEO; ensuring that conflicts of interest among committee members are identified and avoided; appointing independent remuneration consultants; and maintaining appropriate communication with shareholders on the subject of remuneration?”*

#### Guidance 3.6

It would be advantageous to include reference to the disclosure of a board Diversity Policy. For example, *“Is the board’s approach to diversity described in a publicly disclosed Diversity Policy including measurable targets and a time period over which such targets will be achieved?”*

#### Guidance 3.7

The reference to board evaluation is welcomed and ICGN recommends this is extended to refer to the need for individual board directors, including the Chairman, to also be subject to board evaluation.

Furthermore, there should be reference to whether or not an external board evaluation is conducted by an independent outside consultant periodically. For example this could be included in the Guidance as follows: *“Is an external board*

*evaluation conducted by an independent outside consultant conducted periodically to help inform candidates of strategic relevance to the company?”*

#### Guidance 3.9

The reference to board director refreshment is welcomed. We suggest the following is also added to the Guidance: *“Does the board disclose the process for director nomination and election/re-election along with relevant information about the candidates?”*

#### Guidance 3.10

The reference to the role of independent directors is welcomed and the following words underlined are suggested: *“Do independent directors recognize their roles and responsibilities, and provide advice and monitor management appropriately to allow for objective board decision-making in response to business issues and in alignment with the company’s vision, mission and strategy?”*

#### **Matters not included in the Guidelines**

It is noted that the following ICGN recommendations were not included in the latest draft Guidelines:

- Is the incumbent CEO involved in the appointment of his or her successor and, if so, to what extent did this influence the decision-making process?
- Is the CEO also the Chairman / President and, if so, has the rationale for why it is strategically necessary been adequately explained to shareholders? Does the company explain why CEO succession to chairmanship is in the best interests of the company?
- Is one of the Independent Directors appointed the responsibility to be a main point of contact with shareholders?

While we recognise that corporate governance practices take time to evolve in any market, we would encourage continued dialogue around the above questions.

To conclude, ICGN congratulates the leadership of the FSA and the Council once again on the progress that is being made in Japan in terms of corporate governance and investor stewardship reform. I wish you a successful Council Meeting on the 13<sup>th</sup> March and respectfully submit this letter for your kind consideration.

Yours sincerely,



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