

Revising the Code of Corporate Conduct

(Supplementary Materials to Previous Council)

Tokyo Stock Exchange Listing Department

May 21, 2024



- At the previous Council, we received the following comments on conducting an **overall review of the Code of Corporate Conduct in light of changes in the external environment since its establishment in 2007.**
 - **Matters to be Observed should be prioritized** for consideration.
 - When doing so, current stipulations should be maintained as necessary from the perspective of **regulating abusive conduct that undermines the functioning of the market and shareholder rights.**
 - In line with this, given that the **numbers of MBOs and conversions of listed subsidiaries into wholly-owned subsidiaries by controlling shareholders** (hereinafter referred to as "subsidiary conversions"), in particular, **are expected to increase further, the need for additional measures to protect the rights of minority shareholders should be considered as a priority.**
- There was also a point made about the need for **additional analysis** of recent cases of MBOs and subsidiary conversions with regard to aspects like **offer prices and share price movements before the announcement of the action**, to provide a basis for the above consideration.



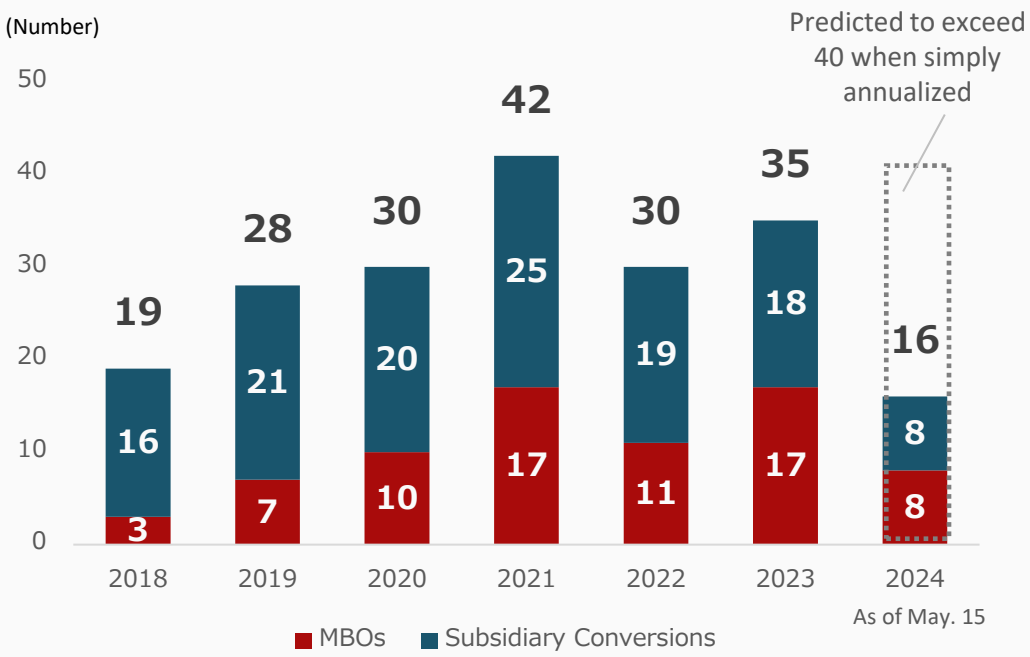
- Today, we will report on our additional analysis.
- We would like for the Council to comprehensively discuss the provisions in the Matters to be Observed, including potential specific action with regards to MBOs and subsidiary conversions, from the next meeting.
- Please let us know any comments or suggestions you may have about the content of the analysis and how to proceed.

Numbers of MBOs/Conversions and Distribution of Takeover Premiums



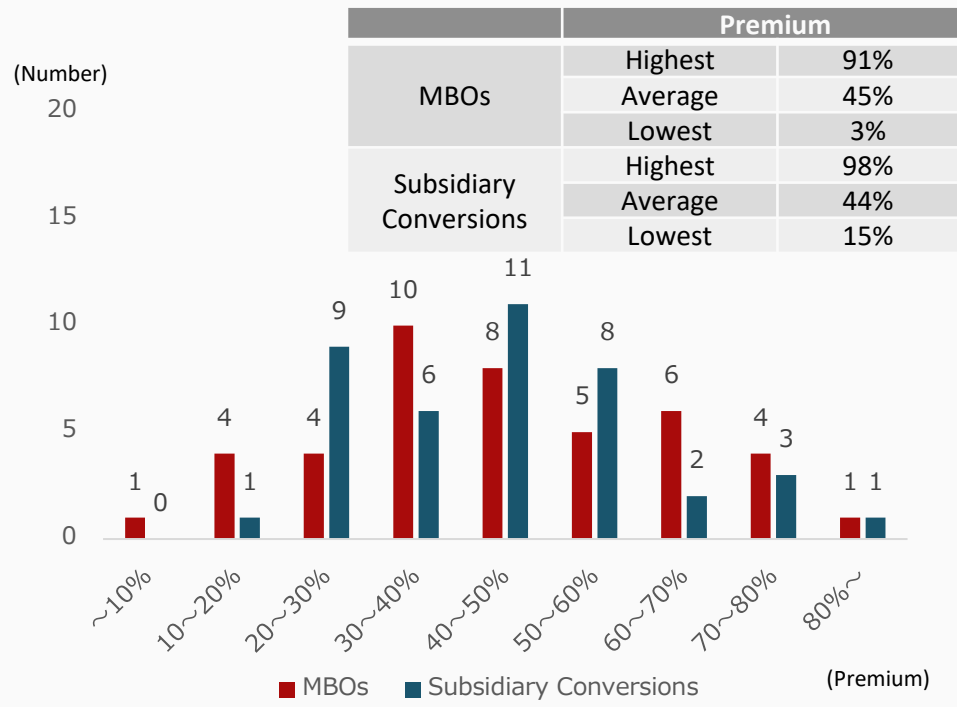
- Numbers of MBOs and subsidiary conversions are **consistently high**.
- **Takeover premiums** are on **average around 40%** of the average market share price before the announcement.
 - During the period surveyed, there were **no cases of buyouts made at prices below the average pre-announcement share price** (that is, no cases which would have violated price restrictions established in other countries as shown on slide 4)

Numbers of Recent MBOs/
Subsidiary Conversions Disclosed



Note: Includes one failed MBO in 2019 (KOSAIDO), one failed MBO in 2020 (Japan Asia Group) , one failed Subsidiary Conversion in 2020 (TOA OIL) and four failed MBOs in 2021 (SAKAI OVEX, KOYOSHA, PiPEDO HD, Katakura Industries)

Distribution of Premiums for MBOs/
Subsidiary Conversions (2021-2023)



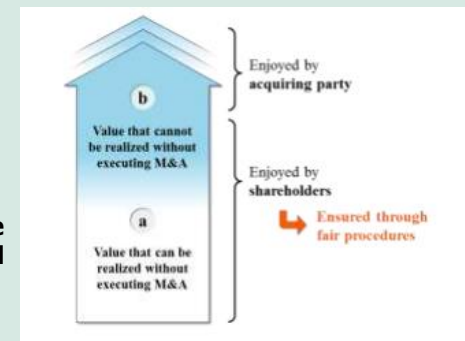
- Notes:
1. Includes MBOs/subsidiary conversions disclosed from 2021 to 2023
 2. Premiums are based on the average market share price in the month from the business day before the day of disclosure
 3. Excludes cases such as where the share price has been influenced by early media reports or other factors before the disclosure date, and those made through share exchanges

2.2 Basic Issues Regarding Acquisition Consideration

2.2.1 Concepts Regarding the Value Realized in M&A

Theoretically, the value realized in an M&A transaction can be separated into two types: (a) value that can be realized without executing the M&A transaction, and (b) value that cannot be realized without executing the M&A transaction.¹⁴

The values of (a) and (b) above should be enjoyed by all shareholders in accordance with the number of shares held by each shareholder. In cases where an M&A transaction is conducted through a squeeze out of general shareholders, theoretically and conceptually, **value that can be realized without executing the transaction (case (a) above) should be enjoyed by all shareholders, including general shareholders in accordance with the number of shares held by such shareholders.**¹⁵ On the other hand, **with respect to value that cannot be realized without executing the transaction (case (b) above), although general shareholders will be squeezed out by the transaction, it is fair that general shareholders should also enjoy an appropriate portion of such value.**¹⁶



2.2.2 Discussion of Actual Cases

As described above, although value realized in M&A transactions can be conceptualized, it is difficult in actual cases to strictly and objectively distinguish and determine the values of (a) and (b) above, as well as to determine to what extent the value of (a) is reflected in the market price before an M&A transaction is announced.¹⁷ In addition, with respect to the value of (b), there is a certain range in the value that general shareholders should enjoy, and it is difficult to create a singular and objective standard for determining what portion should be allocated to general shareholders. Therefore, it is difficult to establish directly a methodology for determining reasonable acquisition consideration in actual cases based on the theoretical concept described above, or to establish any singular or objective criteria such as, “the premium is fair if over x%” compared with the market price of the shares. Therefore, it is not appropriate to establish any singular or objective criteria for transaction terms, including the acquisition consideration; instead, **guidance should be provided with respect to procedures to ensure the fairness of transaction terms (such procedures are hereinafter referred to as “fair procedures”) and, by executing M&A transactions in accordance with such procedures, that general shareholders secure the fair return that they deserve (such returns are hereinafter referred to as the “returns deserved by general shareholders” or the “interests of general shareholders”).** (Omitted)

- 14 In MBOs, theoretically, synergies such as those that occur in business combinations do not occur just as the result of the MBO, but cost reduction effects resulting from the removal of general shareholders (i.e., the elimination of costs related to mediating the interests of general shareholders and disclosure costs), and value created through the efforts of management who contribute human capital in MBOs as a result of changes in incentive structures, are considered to be included in the value of (b), which cannot be realized without executing the M&A transaction. In addition, in the case of MBOs in which management jointly conduct transactions with investment funds, management efficiencies generated through the support of the investment funds and synergies generated with other operating companies under the control of the investment funds may also be included in the value of (b).
- 15 For example, **profits from the sale of idle assets with large unrealized gains can be achieved without executing an M&A transaction, and should be enjoyed by all shareholders rather than monopolized by acquiring parties.** In addition, **value expected to be realized through business alliances with other companies after the M&A transaction can be distinguished in terms of whether such business alliance could be realized through an M&A transaction or could be formed without the M&A transaction theoretically (although it is difficult to determine in practice).** In the latter case, value should not be monopolized by acquiring parties, and should be enjoyed by all shareholders.
- 16 Under the Companies Act, the purchase price of shares in appraisal litigation (i.e., litigation with respect to the rights of dissenting shareholders to demand that a target company purchase their shares at a fair price) in connection with a corporate reorganization is determined to be a “fair price” (such as Article 785 Paragraph 1 of the Companies Act). Such price is interpreted as: (i) the price of the shares held on the record date where the corporate reorganization resulted in an increase in corporate value and, assuming the corporate reorganization was conducted under fair transaction terms, where that increase will be fairly distributed to the shareholders of the respective companies on the record date, and (ii) if the corporate reorganization did not result in an increase in corporate value, the price of shares that would have been held on the record date if there had been no resolution at the general meeting of shareholders approving the corporate reorganization. The prices to be determined by the courts in the case of a cash-out of shareholders by methods other than corporate reorganization are also similarly interpreted.
- 17 **Value that can be realized through the application of existing management resources held prior to the M&A transaction is included in the value of (a), which can be realized without executing the M&A transaction, even if the value is not actually realized.** In this respect, it has been observed that although the value of (a) is expected to be fully realized prior to the delisting of a target company through an MBO or an acquisition of a controlled company by the controlling shareholder, it is often not fully realized during the period in which the company continues as a listed company, and this situation is the basis for price formation in the stock market.

(Ref.) Price Restrictions on Takeovers in Other Countries

- In Europe, **price restrictions for takeover bids have been introduced in laws and regulations, generally setting as the lower limit the maximum consideration the bidder has paid for said security within a certain period, or the market average share price.**

	U.S.	U.K.	Germany	France	Japan
Minimum Price Restriction	Not set*	Set (The maximum amount paid by the bidder in the last 3 months, or the last 12 months in the case of a mandatory offer)	Set (The maximum amount paid by the bidder in the last 6 months or the weighted average share price in the 3 months prior to the announcement)	Set (The maximum amount paid by the bidder in the last 12 months for a mandatory offer, or for a voluntary offer where the bidder already owns 50% or more, the weighted average share price in the 60 days prior to the announcement)	Not set (lowering the purchase price after the bid is prohibited)

*In the U.S., equality between shareholders and price fairness is ensured through rules such as the Best Price Rule and All-Holders Rule. These also have a certain amount of influence over the minimum price. (Best Price Rule: consideration offered to any security holder must be equal to the highest consideration paid to any other security holder; All-Holders Rule: a tender offer must be made available to all shareholders holding the type of shares being solicited for purchase)

(Ref.) Other Regulations/Practices Related to Ensuring Fairness

	U.S.	U.K.	Germany	France	Japan*
Establishment of Special Committee	Normally established under directors' fiduciary duty obligation (composed of the company's independent directors)	No equivalent practice	No equivalent practice	No equivalent practice	Normally established (composed of the company's independent officers, etc.)
Obtaining a Fairness Opinion	Fairness opinion normally obtained under directors' fiduciary duty obligation	While not a "fairness opinion," obtaining an opinion from an independent advisor about the fairness/reasonableness of the economic terms is mandatory	While not mandatory, a fairness opinion is often obtained from a chosen independent advisor (in around half of cases according to past surveys)	Companies must obtain a fairness opinion from a chosen independent expert	Limited cases of a fairness opinion being obtained voluntarily (obtaining a calculation report is mandatory under the listing rules)
MOM Conditions	MOM condition normally set under directors' fiduciary duty obligation	Requirement to acquire 90% or more of the total number of shares subject to the offer (excluding those already held) – more stringent than an MOM	No MOM concept	No MOM concept	Limited cases of MOM conditions being set voluntarily for MBOs (not usually set for subsidiary conversions)
Proactive Market Check	Market check usually carried out under directors' fiduciary duty obligation	No equivalent practice	No equivalent practice	No equivalent practice	Limited cases of proactive market checks being carried out voluntarily

*In the Ministry of Economy, Trade and Industry's "Fair M&A Guidelines," measures such as special committees, obtaining fairness opinions, setting MOM conditions, and proactive market checks are given as possible measures to ensure fairness (to be chosen appropriately depending on each specific situation)

(Sources) METI, survey of overseas legal systems regarding M&A with conflicts of interest (interim report) (White & Case LLP)

METI, FY2021 survey commissioned to Industrial Economic Research "Survey on Corporate Governance Reform in Japan and Abroad"

METI, FY2022 survey commissioned to Industrial Economic Research "Survey on Overseas M&A Regulation (survey report on listed company M&A rules and market trends in the U.S., U.K., Germany, and France)"

OECD, Corporate Governance Factbook 2023

Recent Failed MBOs

- In recent years, there have been **some cases where TOBs for the purpose of an MBO have been unsuccessful.**
- ✓ In the surveyed period (2021 to 2023), there were no cases of failed subsidiary conversions.

Recent Failed MBOs (2021-2023)

Announced	Target Company	Details	Bidder's Holding Ratio*
Feb. 2021	Sakai Ovex (first offer)	- The management of Sakai Ovex conducted a TOB for the purpose of an MBO (raising the offer price from JPY 2,850 to JPY 3,000 midway as the market price held above the TOB price), but it failed as it did not meet the minimum limit (3.93 million shares tendered against a minimum of 4.12 million). (A further TOB (offer price JPY 3,810) was later conducted and accepted.)	14.6%
Mar. 2021	Koyosha	- The management of Koyosha began a TOB for the purpose of an MBO (offer price JPY 935). - CYBRIDGE, which increased its holding to 5% after the TOB, requested a revision of the TOB price (to JPY 1,294) claiming that the price calculation was done by arbitrary methods (that it excluded a comparison with similar companies, etc.) - After negotiations, the TOB price was revised to JPY 1,060, and a tender agreement was signed with CYBRIDGE, but it still failed as it did not meet the minimum limit (300,000 shares tendered against a minimum of 470,000).	23.9%
Sept. 2021	PIPEDO HD (first offer)	- The management of PIPEDO HD (with Advantage Partners) conducted a TOB (offer price JPY 2,800) for the purpose of an MBO, but it failed as it did not meet the minimum limit (310,000 shares tendered against a minimum of 1.83 million). (A further TOB (same offer price at JPY 2,800 – a raise was refused despite a request from the special committee) was later conducted and accepted.)	35.6%
Nov. 2021	Katakura Industries	- The management of Katakura Industries conducted a TOB for the purpose of an MBO (offer price JPY 2,150). - Kagoshima East India Limited (which obtained its shares from Oasis Management Company, the largest shareholder, at JPY 2,350) expressed the opinion that the price was "significantly low considering the market value of the company's real estate holdings," and the TOB failed as it did not meet the minimum limit (19.67 million shares tendered against a minimum of 22.14 million).	0.5%

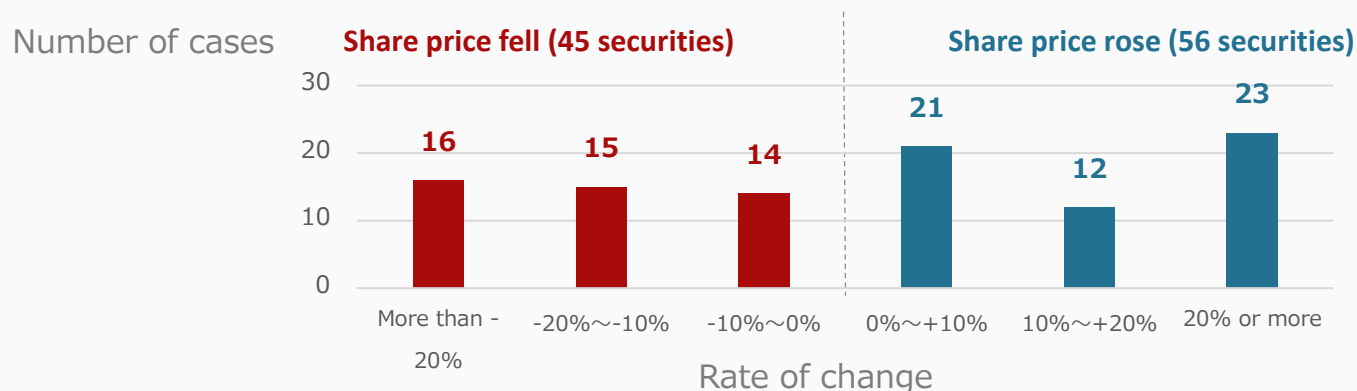
*Includes shares held by others noted on the TOB disclosure as having a material interest, such as tender agreement counterparties

Note: Includes MBOs/subsidiary conversions disclosed from 2021 to 2023

Share Price Movements Before Takeover Disclosure

- Across the surveyed MBOs/subsidiary conversions, there were **no extreme drops in share prices before the timing of disclosure**.
 - Roughly half of securities saw their share price rise in the 250 business days before disclosure, and roughly half saw it fall.
 - There were no significant trends even when split into smaller periods (the mean and median rates of change before disclosure were both positive).

Share Price Trends in the 250 Business Days Before Disclosure (2021 – 2023)



Share Price Trends by Period

	Business days before disclosure				
	250	200	100	30	7
Share price rose	55%	51%	54%	62%	60%
Share price fell	45%	49%	46%	38%	40%
Rate of change (mean)	+5.5%	+4.1%	+4.3%	+2.7%	+0.9%
Rate of change (median)	+1.0%	+0.3%	+1.5%	+1.3%	+0.3%

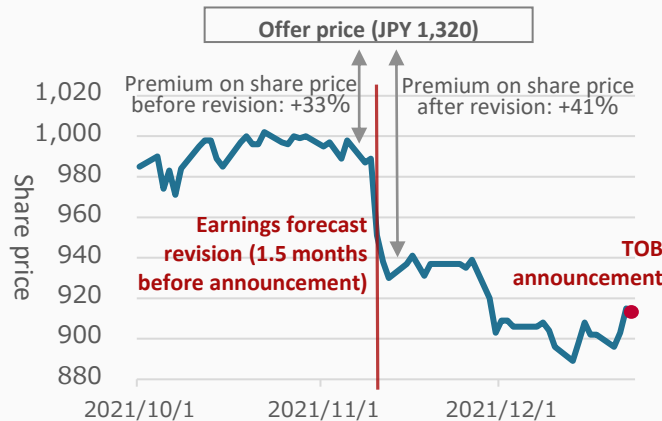
Note: 1. Includes MBOs/subsidiary conversions disclosed from 2021 to 2023

2. Excludes cases where the share price has been influenced by early media reports or other factors before the disclosure date

(Ref.) Cases of Negative Information Disclosed Before Takeover

- There have been cases of MBOs/subsidiary conversions being carried out after significant downward revisions of financial results.
 - Given that a **downward revision of financial results just before an MBO/subsidiary conversion announcement could invite suspicion of deliberate lowering of the market share price to facilitate acceptance of the offer**, METI's Fair M&A Guidelines ask for a **detailed explanation of aspects such as the background and purpose of conducting the MBO/subsidiary conversion at that specific time**.

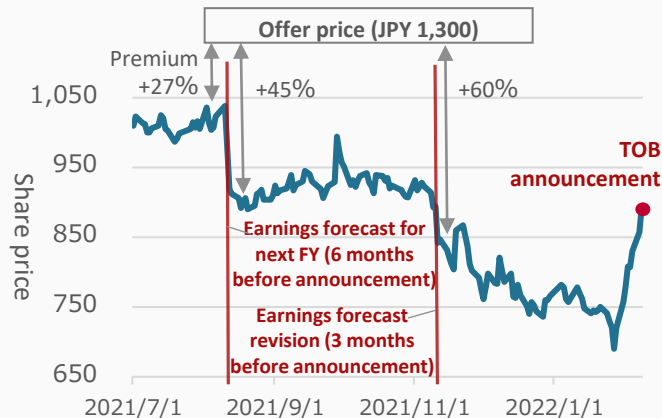
- ✓ Downward revision of earnings forecast (profit for FY down approx. 65%)



Our company published a press release regarding a discrepancy in the forecast and actual financial results for Q2 as well as a revision to the full fiscal year results forecast on November 10, 2021, and carried out a downward revision of its consolidated earnings forecast for the fiscal year ending March 2022, after receiving a proposal regarding the synergies, scheme, and schedule for the transaction from the offeror on October 20, 2021. However, this revision was due to sluggish orders in the engineering business, especially in Japan in the first half of the year, and a prediction in the pipe and materials business that a decrease in income was unavoidable due to rising oil and lead prices, among other things, as well as a decrease in sales due to a decrease in orders. The revision was therefore disclosed in line with Tokyo Stock Exchange's timely disclosure standards, and was not related to this transaction or made with this transaction in mind.

(Based on published materials regarding the buyout by the controlling shareholder, December 21, 2021)

- ✓ Earnings forecast (profit for Q down 30% YoY) and downward revision of earnings forecast (profit for the FY down approx. 60%)



Given that a) the company published both the earnings forecast for the quarter ending June 2022 on August 10, 2021, and the downward revision of the earnings forecast on November 11, 2021, before the planned board of directors' resolution; b) said earnings forecast was created using the same methods and procedures as in any other year; and c) said downward revision was published in line with the company's internal rules based on the actual results at the time, the Special Committee saw nothing that would suggest anything unreasonable in this series of events. Since, based on this, the Special Committee saw nothing in either the earnings forecast or the downward revision that would suggest that, for example, they were created and published to deliberately bring down the company's market share price, it can be considered reasonable to refer to the company's market share price after the above publication dates in consideration of the TOB price.

(Based on published materials regarding the MBO, February 9, 2022)

Approach to MBOs and Provisions in the Code of Corporate Conduct

- MBOs and subsidiary conversions play an important role in maintaining a vibrant capital market by allowing companies that have completed their role as a listed company to **exit the market, improving management flexibly**, and providing shareholders with a **chance to obtain a premium for their shares**.
- **On the other hand, given the existence of problems of structural conflicts of interest and information asymmetry**, TSE has put in place provisions mostly in the Code of Corporate Conduct's "Matters to be Observed" from the following perspectives:
 - **Establishing an environment** where general shareholders can **make appropriate judgments based on necessary and sufficient information regarding the appropriateness of the transaction's terms** and other aspects
 - **Promoting the setting of fair transaction terms through ensuring fair procedures**

	MBOs	Subsidiary Conversions
Information disclosure	Requirement for necessary and sufficient timely disclosure (effectiveness of the Special Committee, important assumptions for the share value calculation, independence of the calculation agent, etc.)	
Obtaining a calculation report	Requirement for obtainment and disclosure of a summary of a calculation report which includes the view of a third party with expertise or experience in the valuation of corporate value or stock on the price of the offer, etc. (Obtainment/disclosure of a summary is also required from listed parent companies that are controlling shareholders)	
Obtaining an opinion that the transaction will not undermine the interests of minority shareholders (applicable to all material transactions involving controlling shareholders)	No provisions In practice, it is normal for a Special Committee to advise on whether the transaction will undermine the interests of minority shareholders, and for the company to obtain and disclose a summary of a report regarding this, like in the case of subsidiary conversions.	Requirement to obtain an opinion* from an entity that has no interest in the controlling shareholder that the transaction will not undermine the interests of minority shareholders (disclosure of a summary only) *A statement that the decision will not undermine the interests of minority shareholders, based on a comprehensive review of such aspects as the purpose of the transaction, the negotiation procedures (the process of selecting the calculation agent, the involvement of outside directors or outside auditors in the decision-making process, etc.), the fairness of the consideration, and enhancing the corporate value of the listed company.

(Ref.) Timely Disclosure on Takeovers (1)

- The Guidebook for the Timely Disclosure of Corporate Information gives the following with regard to the **necessary and sufficient timely disclosure about MBOs/subsidiary conversions** required in the Code of Corporate Conduct.
- In addition, disclosure about aspects such as the **effectiveness of Special Committees and the independence of calculation agents is progressing** based on METI's Fair M&A Guidelines.
 - However, cases of more detailed disclosure on assumptions for the share value calculation including the information suggested in the Fair M&A Guidelines (approach to the predicted free cash flow period, approach to the perpetual value such as the growth rate, etc.) are limited.

	Timely Disclosure Guidebook	(Ref.) Fair M&A Guidelines
Information on the Special Committee	<p>(If a special committee is established)</p> <ul style="list-style-type: none"> ➤ Outline of the special committee (names/occupations of members, etc.) ➤ If the committee gave advice on the announcement of opinion, the contents of that advice and the response to that advice ➤ If the committee was commissioned to negotiate with the offeror, a statement to that effect <p>(When obtaining an opinion from a special committee, etc. in the case of a subsidiary conversion)</p> <ul style="list-style-type: none"> ➤ Outline of the opinion stating that the bid is not disadvantageous to minority shareholders (including date of obtainment, giver of opinion, contents (including reasons for the opinion)) 	<ul style="list-style-type: none"> ➤ Suitability of committee members, such as independence and qualifications (independence, attributes/reasons for appointment, selection process, etc.) ➤ Scope of authority granted to Special Committee (involvement in transaction terms negotiation process with acquiring party, appointment of advisors, etc.) ➤ Process of deliberations at the Special Committee, status of involvement in transaction terms negotiation process with acquiring party (timing of establishment, matters reviewed, information received, number and duration of meetings, etc.) ➤ Basis for and rationale behind Special Committee's judgement on the appropriateness of the transaction terms and fairness of procedures of the M&A, and whether it should proceed (results of evaluations on principal matters evaluated regarding the M&A, and basis/rationale behind these) ➤ Information on remuneration structure for committee members

(Ref.) Timely Disclosure on Takeovers (2)

	Timely Disclosure Guidebook	(Ref.) Fair M&A Guidelines
Information on the share value calculation (important assumptions for the calculation)	<p>(When using the DCF method)</p> <ul style="list-style-type: none"> ➤ Specific figures for the financial projections on which the calculation is based <ul style="list-style-type: none"> – If these include a significant increase or decrease, the reasons for this ➤ Sources for the financial projections on which the calculation is based ➤ Whether the financial projections assume that the transaction in question will take place ➤ Specific figures for discount rates ➤ Calculation methodology for going concern value and specific parameters used in the calculation ➤ Other special preconditions, if any 	<p>(When using the DCF method)</p> <ul style="list-style-type: none"> ➤ Free cash flow forecasts for the target company on which the calculation is based <ul style="list-style-type: none"> – Thinking behind the projection period ➤ Chronology of preparation of financial forecasts on which the calculation is based (whether the rationality of the business plan was confirmed by the Special Committee, whether the financial forecasts were reviewed by third-party valuation advisors; if using financial forecasts that differ substantially from those announced before the M&A, the reasons for this; etc.) ➤ Whether the financial forecasts assume that the transaction in question will be carried out ➤ Type and grounds for calculation of discount rate ➤ Perspectives on the perpetual value such as the growth rate, etc. assumed for after the forecast period
Information on the fairness opinion	<ul style="list-style-type: none"> ➤ If a fairness opinion has been obtained from the calculation agent, the contents of said opinion 	<ul style="list-style-type: none"> ➤ Process of issuing the opinion, views on "fairness," etc.
Information on material interest relationships with third-party evaluation organizations	<ul style="list-style-type: none"> ➤ If there is a material interest relationship with a calculation agent (see note), the details of that relationship and why the company requested the calculation from an agent with which it has a material interest relationship <p>(Note) e.g., a) When the agent falls under the definition of a related party; b) when the request is given to an agent recommended or introduced by the offeror (including the offeror's shareholders, officers, financial advisors, or other similar parties); c) when the agent receives requests from both the listed company and the offeror; d) when the company or any of its related companies (including subsidiaries) are receiving financing from the agent</p>	<ul style="list-style-type: none"> ➤ Fee structure of third-party valuation advisor (whether the fee is a contingency fee paid on factors such as the completion of the M&A or a fixed fee paid regardless of the M&A's success), etc.

- At the study group looking at how to protect minority shareholders of subsidiary listed companies, the "opinion that the transaction will not undermine the interests of minority shareholders" was also discussed.

Interim Report (September 1, 2020)

2. Clarification of Issues

(2) Issues Highlighted by Recent Cases

In a case at a listed subsidiary, **the board of directors expressed an opinion endorsing a tender offer by its Controlling Shareholder but did not recommend shareholders to tender their shares mainly because the tender offer price proposed by the Controlling Shareholder was below the minimum of the price range calculated by the DCF method in a stock valuation report obtained by a special committee.** There is opinion that although the board of directors of the listed subsidiary obtained a report from the special committee stating that it is appropriate for the board of directors to express an opinion that (i) the board endorsed the tender offer by the Controlling Shareholder and (ii) the decision on whether to tender shares was left to its shareholders,¹ the board of directors cannot be considered to have obtained an opinion that actively expresses that "the interests of minority shareholders will not be undermined."

3. Framework for Minority Shareholder Protection

(2) Procedures

With respect to "opinion on not undermining the interests of minority shareholders" in a tender offer by a Controlling Shareholder aimed at taking a listed subsidiary private, it is increasingly important that a special committee composed of independent directors expresses its opinion from the perspective of protecting minority shareholder interests after the Ministry of Economy, Trade and Industry issued "Fair M&A Guidelines: Enhancing Corporate Value and Securing Shareholders' Interests" (June 28, 2019). In light of the circumstances, there is opinion that **a listed company cannot be considered to have obtained an opinion that actively expresses that "the interests of minority shareholders will not be undermined" even if the company obtains a report from a special committee endorsing a tender offer by a Controlling Shareholder but not recommending shareholders to tender their shares.** There is also opinion that in connection with "opinion on not undermining the interests of minority shareholders," which is required by the listing system as part of the framework for minority shareholder protection, **the special committee could withhold its opinion if it does not recommend shareholders to tender their shares.**²

On the other hand, there is opinion that requiring excessive procedures in such situations may make it difficult for a Controlling Shareholder to implement a tender offer, and accordingly, may lead to minority shareholders being denied the opportunity to receive a premium, which is an undesirable outcome for minority shareholders.³ There is also opinion that requiring excessive procedures may work against the dissolution of parent-subsidiary listings that have no economic rationale.

Therefore, the Study Group will **continue to discuss the framework for minority shareholder protection in situations where a Controlling Shareholder conducts a tender offer aimed at taking a listed subsidiary private, including the essence of "opinion on not undermining the interests of minority shareholders," taking into account the role expected of special committees.**⁴

1 The risk of conflicts of interest between a Controlling Shareholder and minority shareholders is most apparent in a tender offer by the Controlling Shareholder. Therefore, in order to prevent the Controlling Shareholder from abusing its position and to appropriately protect minority shareholders, TSE requires the listed company to obtain "an opinion that the decision will not undermine the interests of minority shareholders" from "an entity that has no interest in the Controlling Shareholder" and to perform necessary and sufficient timely disclosure (Rule 441-2 of the Securities Listing Regulations).

2 However, there is opinion that the fact that the report from the special committee that it does not recommend tendering shares, in a sense, indicates that it is functioning.

3 There is opinion that market checks cannot be expected to function effectively in this situation since the Controlling Shareholder is unlikely to accept a third-party tender offer.

4 In this regard, there is opinion that when a Controlling Shareholder conducts a tender offer aimed at taking its listed subsidiary private, from the perspective of minority shareholder protection, a plausible measure could be to require a majority-of-minority, where the condition for the consummation of such tender offer is that a majority of minority shareholders tenders their shares. On the other hand, there is opinion that requiring a majority-of-minority may impede Controlling Shareholders from conducting tender offers for listed subsidiaries, which would end up working against the interests of minority shareholders.

- Violations of the Code of Corporate Conduct with regards to MBOs/subsidiary conversions are, like for violations of other Matters to be Observed, **subject to measures to ensure effectiveness** (improvement reports, etc.).
- On the other hand, in the case of MBOs/subsidiary conversions, since there are **limits to the functionality of measures such as the above that are based on delisting**, in 2016, TSE discussed and announced additional viewpoints for and points for operation of listing examinations, in view of potential cases where a company that delisted as a result of an MBO might later try to re-list.
 - **At the examination for a re-listing**, TSE looks to confirm **whether there were any minority shareholder protection issues at the time of the MBO/subsidiary conversion, taking into account what has happened since.**

Viewpoints for Examination

Item	Content
1. Relationship between the MBO and the re-listing	<ul style="list-style-type: none"> • Whether the actions are independent of each other or have a close relationship (whether they are led by the same people or connected people, the time between the MBO and the re-listing, etc.)
2. Appropriateness of premium distribution and reasonableness of the MBO	<p>Circumstances at the time of the MBO:</p> <ul style="list-style-type: none"> • Confirmation of whether the procedures at the time of the MBO followed METI's guidelines, etc. <p>Circumstances since the MBO:</p> <ul style="list-style-type: none"> • If there is a discrepancy between the plan at the time of the MBO and the progress since, confirmation of whether a reasonable explanation can be given for this

Operation of Examination

- Given the confirmation of 1. and 2. above, the decision on whether to allow the listing is made after comprehensive consideration of aspects such as whether the company has in place a corporate governance system to prevent actions that would cause investor protection issues after listing, and the explanation and disclosure regarding the background to the re-listing.

(Even if it is judged that there were issues with a past MBO, since these cannot be fixed retroactively, TSE does not automatically refuse all re-listings for this reason.)

Direction of Discussions

- It has been 15 years since the current structure of the Code of Corporate Conduct was established, and **things have changed substantially since then, so I think TSE should review the current stipulations from a clean slate.**
- Since things have changed a lot since 15 years ago, **TSE needs to change the Code to match the times.** The **provisions are quite weak compared to the guidelines for exercising voting rights for institutional investors, so some feel unsuitable** (although you don't necessarily need to match everything to those guidelines).
- TSE needs to separate the **rules-based Code of Corporate Conduct and the principles-based Corporate Governance Code.** From that perspective, the **main part of the Code of Corporate Conduct is the Matters to be Observed.** Discussions should be **centered on the Matters to be Observed and focus on what should be included as a material issue.**
- The **Matters to be Observed are extremely important rules for managing listed companies,** so care should be taken to make sure their position is not undermined.
- The idea of principles-based regulation has not yet permeated into Japan, so **TSE must properly make clear the underlying spirit and stance of the detailed rules.**

Stipulating Necessary Provisions for Improving Mid- to Long-Term Corporate Value

- Since the objectives and formats are different, **it would not be appropriate to simply incorporate all of the Corporate Governance Code's provisions into the "Matters Desired to be Observed."**
- TSE could **include disclosure or other aspects of "Action to Implement Management that is Conscious of Cost of Capital and Stock Price" in the Matters Desired to be Observed.**

"Matters to be Observed" Overall

- The Matters to be Observed have been **implemented with the objective of regulating abusive actions that impede the functioning of the market and the rights of shareholders**. It is not the case that the current provisions are unnecessary because no problems have occurred recently. **TSE must retain in full the provisions regarding actions that are problematic in terms of protecting shareholder rights.**

MBOs/Subsidiary Conversions

- **MBOs and subsidiary conversions are the most important discussion point.** There have been cases that clearly go against METI's guidelines, so **measures are needed in the Matters to be Observed in a way that links to enforcement.**
- **Price appropriateness** is the biggest issue for MBOs. TSE could consider improving the governance around valuations, such as by requiring calculation reports from multiple agents. **As MBOs are expected to increase in the future, advance action is needed.**
- I understand that **METI's guidelines on M&As were aimed at the legal side**, but it would also be possible as the exchange to **update the provisions on the ideal M&A and MBO from an investor protection perspective and include that.**
- As it is **difficult to deal with MBOs using the normal kind of enforcement that leads to delisting**, TSE could introduce regulations like those in other countries such as a lower limit on the price or restrictions on MBOs after the **publication of material negative information.**
- **METI's policies on buyouts have also been substantially revised**, so a review of the Code of Corporate Conduct is also needed in this area.

Appointment of Independent Directors

- **Things have changed substantially since the introduction of the provisions for appointment of independent directors**, so TSE could **perform a review** on this.
- It could be possible to leave the obligation to appoint independent directors to the Corporate Governance Code, but **TSE should strictly maintain the exchange's independence standards.**

Other

- There is a principle in the Corporate Governance Code on **CEO succession plans**, but in practice, some companies have not even created a document. **It should be made clear in the Matters to be Observed that candidates should be given a suitable period of time to study being the management leader before becoming CEO.**
- The **appointment of female officers** is also progressing very slowly in part, so I think it would be good to have more enforceable provisions on this.
- If the focus is going to shift from statutory disclosure to timely disclosure, as happened with quarterly reports before, it will be important to **clarify the spirit of timely disclosure such as why it is important and how companies should approach it, and make sure companies understand this, as an addition to the current detailed disclosure standards.**
- **Shareholder responsibility and fiduciary duty with regards to corporate group management** is also a topic for discussion.