

Revisions to the Rules for Securities on Alert in Order to Improve the Effectiveness of Listed Companies' Improvements to Their Internal Management Systems

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Tokyo Stock Exchange, Inc.

I. Objective

In 2007, Tokyo Stock Exchange, Inc. (TSE) introduced the Rules for Securities on Alert in order to encourage companies that have committed serious violations of TSE's Listing Rules to improve their internal management systems. TSE then made some revisions in 2013 that included shortening the designated period for companies to make such improvements, in order to encourage them to do so more promptly.

An examination of the status of the securities designated as Securities on Alert after the 2013 revisions shows a tendency for companies to complete improvements to their internal management systems more promptly than before the revisions. However, there have been some cases where it came time to conduct the first-year examination before the company had completed developing its system, and the designation had been extended.

Furthermore, there have also been cases where a company's internal management system had shown signs of improvement at the time of the de-designation examination, but because of problems with the company's business continuity, profitability, and other issues, it was thought necessary to regularly check whether the system continued to be adequately maintained and implemented.

In light of these circumstances and in the hope of further increasing the credibility of the securities market, TSE shall make needed revisions to the Rules for Securities on Alert in order to urge listed companies to promptly develop their internal management systems and to enhance the effectiveness of their improved internal management systems in the hope that such systems shall become firmly established.

TSE shall also make revisions to the examination process for market segment transfers and other needed revisions to the listing rules.

II. Overview

Item	Details	Remarks
1. Revisions to Rules		

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for Securities on Alert		
(1) Clarification of De-designation Requirements	<ul style="list-style-type: none"> • The revisions shall make it clear that a listed company shall be de-designated when TSE finds that the company's internal management system is adequately developed and implemented. 	<ul style="list-style-type: none"> • Currently, a listed company is de-designated when TSE can find no problems with the company's internal management system. However, TSE shall make the de-designation requirements clearer in order to urge listed companies to adequately develop and implement their internal management systems. • In addition, the revisions shall make the standpoint of the examination regarding a company's internal management system consistent with that of the initial listing examination for each market segment. • However, please refer to "1. (3) Establishment of a New Follow-Up Period" for the handling of such cases as where TSE finds that the company's internal management system is adequately developed and implemented but cannot confirm whether the company has ensured its business continuity and profitability.
(2) Stricter Timeframe for Development	<ul style="list-style-type: none"> • TSE shall require a listed company with the designation to have an adequately developed internal management 	<ul style="list-style-type: none"> • Under the current rules, TSE shall extend the designation for six months if future

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	<p>system in place by the time of first-year examination.</p>	<p>improvements are likely, even when TSE finds that the company has not adequately developed its internal management system at the time of the first-year examination. However, under the revised rules, TSE shall strictly set the timeframe for developing an internal management system at one year in order to encourage its prompt development. If TSE finds that the company has not adequately developed its internal management system within one year, the company will be delisted.</p> <ul style="list-style-type: none"> • If TSE finds that the company's internal management system is adequately developed but does not find that it is adequately implemented at the time of the first-year examination, TSE will still allow the designation to be extended until the second examination. The second examination shall be conducted in order to check on the status of the development and implementation of the company's internal management system over the past fiscal year. It shall be conducted based on the Written Confirmation of Internal Management System

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		<p>that has been submitted by the listed company within the three-month period following the last day of the fiscal year during which the company's designation was extended based on the first-year examination and shall take the contents of the company's most recent internal control report and internal control audit report into account.</p>
<p>(3) Establishment of a New Follow-Up Period</p>		<ul style="list-style-type: none"> Under the current rules, a listed company is de-designated if TSE can find no problems with the company's internal management system at the time of the examination. However, TSE believes that it is highly likely that a listed company will no longer be able to adequately maintain and implement its the internal management system when, for instance, TSE finds that the listed company has not ensured its business continuity and profitability. Because of this, under the revised rules, TSE shall extend the designation for a period of up to three fiscal years and regularly check on the status of the development and implementation of the listed company's internal management system in the hope that the improvements shall become firmly

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(i) Eligible Companies	<ul style="list-style-type: none"> • TSE will extend the designation of those listed companies whose internal management systems have been found to be adequately developed and implemented by the second examination and to which the cases that have been specified in a. or b. below apply. <ul style="list-style-type: none"> a. Cases where TSE finds that the company has not ensured its business continuity and profitability b. Cases where the company does not meet the continued listing criteria 	<p>established.</p> <ul style="list-style-type: none"> • TSE shall check whether a company has ensured its business continuity and profitability by confirming that there are no notes regarding the going concern assumption in the company's financial statements and related documents. If the company is listed on the Prime Market or the Standard Market, TSE shall also confirm that the company meets the initial listing criteria for profit and net assets that TSE has set as the level at which stable business operations can be conducted in each market segment.
(ii) Handling of the Examinations and the Items to be Confirmed	<ul style="list-style-type: none"> • After the end of each fiscal year, TSE shall examine the status of the development and implementation of the internal management systems of listed companies that fall under "(i) Eligible Companies" and that have had their designations extended. It shall then make a determination as follows. <p>(First and Second Fiscal Years)</p> <ul style="list-style-type: none"> a. When TSE finds that the company has adequately developed and implemented its internal management system, and the company no longer falls under "(i) 	<ul style="list-style-type: none"> • TSE shall conduct the examination for the respective fiscal year based on the Written Confirmation of Internal Management System that has been submitted by the listed company within the three-month period following the last day of that fiscal year. • In addition, TSE shall conduct an interim examination to see whether a company's internal management system has been adequately developed and implemented when it deems that such an examination is necessary.

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	<p>Eligible Companies”</p> <p>De-designation</p> <p>b. When TSE finds that the company has adequately developed and implemented its internal management system, and the company falls under “(i) Eligible Companies”</p> <p>Extension of Designation</p> <p>c. When TSE finds once again that the company has not adequately developed and implemented its internal management system</p> <p>Delisting</p> <p>(Third Fiscal Year)</p> <p>a. When TSE finds that the company has adequately developed and implemented its internal management system</p> <p>De-designation</p> <p>b. When TSE finds once again that the company has not adequately developed and implemented its internal management system</p> <p>Delisting</p>	<p>TSE shall conduct the interim examination in such cases as (1) where the company has committed a new, serious violation of the Financial Instruments and Exchange Act or TSE’s Listing Rules or (2) where TSE finds a huge disparity between such things as the management organization and the internal rules that the company has developed and their actual implementation.</p> <ul style="list-style-type: none"> • During the examination, TSE will also check whether the company has adequately updated and implemented its internal management system in response to any environmental changes that have occurred, such as a major business overhaul or a change of parent companies. • When a listed company that falls under “(i) Eligible Companies” and has had its designation extended applies for a segment transfer and passes the segment transfer examination, TSE shall consider that to mean that it has confirmed that the listed company has adequately developed and implemented its internal

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		<p>management system and ensured its business continuity and profitability and shall de-designate the listed company on the date of the segment transfer.</p>
<p>(iii) Disclosure of the Status of the Development and Implementation of a Listed Company's Internal Management System</p>	<ul style="list-style-type: none"> • A listed company that falls under “(i) Eligible Companies” and has had its designation extended shall disclose the status of the development and implementation of its internal management system at least once a year in principle. 	<ul style="list-style-type: none"> • The listed company shall make the disclosure within the three-month period following the last day of the fiscal year during which the company's designation was extended. Please note that the listed company shall disclose any changes in the status of the development of its internal management system that are based on environmental or other changes that have occurred, such as a major business overhaul or a change of parent companies. • Furthermore, in addition to its regular disclosures, the listed company shall make any other disclosures that TSE deems necessary. • From the standpoint of ensuring the effectiveness of improvements to its internal management system, the listed company shall also disclose its efforts and progress toward improving any problems with its business continuity, profitability, or other issues.

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(4) Other		
(i) Name Change	<ul style="list-style-type: none"> The current “Securities on Alert” shall be renamed to “Securities on Special Alert.” 	<ul style="list-style-type: none"> While the rules’ basic functions shall remain the same, the name shall be changed to make it easier for investors to understand.
(ii) Establishment of New Rules Regarding Post-de-designation Status Reports	<ul style="list-style-type: none"> TSE may require a listed company that was de-designated to submit Improvement Status Reports for a period of five years after the de-designation. The Improvement Status Reports shall describe the status of the development and operation of the company’s internal management system. 	<ul style="list-style-type: none"> The submitted Improvement Status Reports shall be made available for public inspection.
2. Other		
(1) Streamlining the Segment Transfer Examination Process	<ul style="list-style-type: none"> When a listed company in the Prime or Growth Market intends to transfer to the Standard Market, it shall be eligible for TSE’s segment transfer examination, even if it has not undergone a listing eligibility examination by a managing trading participant. 	<ul style="list-style-type: none"> TSE will make this revision as part of an effort to streamline the examination process. This is because, based on the market segment concept, the examination for segment transfer to the Standard Market has relatively fewer items to be checked than those for segment transfer to the Prime or Growth Markets, and because TSE can also take the listed company’s past performance into account. Since TSE anticipates that the number of items it has to check may increase when the listed

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		company has not undergone a listing eligibility examination, it will not set a standard examination period.
(2) Other	• Other necessary revisions shall be made.	

III. Implementation Schedule (Planned)

Implementation is scheduled for January 2024.

Items 1. (1) to 1. (3) shall apply to companies that are designated as Securities on Special Alert on or after the effective date.

Item 1. (4) (ii) shall apply to companies that are de-designated as Securities on Special Alert on or after the effective date.

Item 2. (1) shall apply to companies that apply for a segment transfer on or after the effective date.

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