

Revision of Japan's Corporate Governance Code based on the proposal of the Council

March 30, 2018
Tokyo Stock Exchange, Inc.

I. Purpose

The Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code (the "Council") handled jointly by the Financial Services Agency and Tokyo Stock Exchange ("TSE") has made proposals to revise the Corporate Governance Code in order to deepen and make more substantive Japan's corporate governance reform through engagement between investors and companies. In accordance with these proposals, TSE will make the necessary revisions to the Securities Listing Regulations.

II. Outline

Item	Contents	Remarks
Revision of the Code	<ul style="list-style-type: none">TSE shall revise Japan's Corporate Governance Code as attached.	<ul style="list-style-type: none">Listed companies shall submit their corporate governance reports immediately after the preparation of the revised version thereof, but not later than the end of December 2018.

III. Implementation Date (Scheduled)

The revised Japan's Corporate Governance Code will be implemented in June 2018.

※ For reference, the "Revision of the Corporate Governance Code and Establishment of Guidelines for Investor and Company Engagement" proposed by the Council and the "Guidelines for Investor and Company Engagement (Draft)" drafted by the Financial Services Agency are attached.

Provisional translation

Japan's Corporate Governance Code

**Seeking Sustainable Corporate Growth and Increased Corporate Value
over the Mid- to Long-Term**

(Draft Revision)



March 30, 2018

Tokyo Stock Exchange, Inc.

Japan's Corporate Governance Code

In this Corporate Governance Code, “corporate governance” means a structure for transparent, fair, timely and decisive decision-making by companies, with due attention to the needs and perspectives of shareholders and also customers, employees and local communities.

This Corporate Governance Code establishes fundamental principles for effective corporate governance at listed companies in Japan. It is expected that the Code's appropriate implementation will contribute to the development and success of companies, investors and the Japanese economy as a whole through individual companies' self-motivated actions so as to achieve sustainable growth and increase corporate value over the mid- to long-term.

General Principles

Securing the Rights and Equal Treatment of Shareholders

1. Companies should take appropriate measures to fully secure shareholder rights and develop an environment in which shareholders can exercise their rights appropriately and effectively.

In addition, companies should secure effective equal treatment of shareholders.

Given their particular sensitivities, adequate consideration should be given to the issues and concerns of minority shareholders and foreign shareholders for the effective exercise of shareholder rights and effective equal treatment of shareholders.

Appropriate Cooperation with Stakeholders Other Than Shareholders

2. Companies should fully recognize that their sustainable growth and the creation of mid- to long-term corporate value are brought as a result of the provision of resources and contributions made by a range of stakeholders, including employees, customers, business partners, creditors and local communities. As such, companies should endeavor to appropriately cooperate with these stakeholders.

The board and the management should exercise their leadership in establishing a corporate culture where the rights and positions of stakeholders are respected and sound business ethics are ensured.

Ensuring Appropriate Information Disclosure and Transparency

3. Companies should appropriately make information disclosure in compliance with the relevant laws and regulations, but should also strive to actively provide information beyond that required by law. This includes both financial information, such as financial standing and operating results, and non-financial information, such as business strategies and business issues, risk, and governance.

The board should recognize that disclosed information will serve as the basis for constructive dialogue with shareholders, and therefore ensure that such information, particularly non-financial information, is accurate, clear and useful.

Responsibilities of the Board

4. Given its fiduciary responsibility and accountability to shareholders, in order to promote sustainable corporate growth and the increase of corporate value over the mid- to long-term and enhance earnings power and capital efficiency, the board should appropriately fulfill its roles and responsibilities, including:
- (1) Setting the broad direction of corporate strategy;
 - (2) Establishing an environment where appropriate risk-taking by the senior management is supported; and
 - (3) Carrying out effective oversight of directors and the management (including *shikkoyaku* and so-called *shikkoyakuin*) from an independent and objective standpoint.

Such roles and responsibilities should be equally and appropriately fulfilled regardless of the form of corporate organization – i.e., Company with *Kansayaku* Board (where a part of these roles and responsibilities are performed by *kansayaku* and the *kansayaku* board), Company with Three Committees (Nomination, Audit and Remuneration), or Company with Supervisory Committee.

Dialogue with Shareholders

5. In order to contribute to sustainable growth and the increase of corporate value over the mid- to long-term, companies should engage in constructive dialogue with shareholders even outside the general shareholder meeting.

During such dialogue, senior management and directors, including outside directors, should listen to the views of shareholders and pay due attention to their interests and concerns, clearly explain business policies to shareholders in an understandable manner so as to gain their support, and work for developing a balanced understanding of the positions of shareholders and other stakeholders and acting accordingly.

Section 1: Securing the Rights and Equal Treatment of Shareholders

General Principle 1

Companies should take appropriate measures to fully secure shareholder rights and develop an environment in which shareholders can exercise their rights appropriately and effectively.

In addition, companies should secure effective equal treatment of shareholders.

Given their particular sensitivities, adequate consideration should be given to the issues and concerns of minority shareholders and foreign shareholders for the effective exercise of shareholder rights and effective equal treatment of shareholders.

Notes

Companies have various stakeholders, including shareholders. Without appropriate cooperation with these stakeholders, it would be difficult for companies to achieve sustainable growth. Suppliers of capital are an important cornerstone, and shareholders are the primary starting point for corporate governance discipline. Companies should secure appropriate cooperation with shareholders and strive toward the achievement of sustainable growth by fully securing shareholder rights and providing for the smooth exercise thereof.

In addition, the Companies Act requires companies to equally treat shareholders based on the class and number of shares they hold. Gaining broad confidence of shareholders that they receive equal treatment will also contribute to strengthening support from the suppliers of capital.

Principle 1.1 Securing the Rights of Shareholders

Companies should take appropriate measures to fully secure shareholder rights, including voting rights at the general shareholder meeting.

Supplementary Principles

- 1.1.1 When the board recognizes that a considerable number of votes have been cast against a proposal by the company and the proposal was approved, it should analyze the reasons behind opposing votes and why many shareholders opposed, and should consider the need for shareholder dialogue and other measures.
- 1.1.2 When proposing to shareholders that certain powers of the general shareholder meeting be delegated to the board, companies should consider whether the board is adequately constituted to fulfill its corporate governance roles and responsibilities. If a company determines that the board is indeed adequately constituted, then it should recognize that such delegation may be desirable from the perspectives of agile decision-making and expertise in business judgment.
- 1.1.3 Given the importance of shareholder rights, companies should ensure that the exercise of shareholder rights is not impeded. In particular, adequate consideration should be given to the special rights that are recognized for minority shareholders with respect to companies and their officers, including the right to seek an injunction against illegal activities or the right to file a shareholder lawsuit, since the exercise of these rights tend to be prone to issues and concerns.

Principle 1.2 Exercise of Shareholder Rights at General Shareholder Meetings

Companies should recognize that general shareholder meetings are an opportunity for constructive dialogue with shareholders, and should therefore take appropriate measures to ensure the exercise of shareholder rights at such meetings.

Supplementary Principles

- 1.2.1 Companies should provide accurate information to shareholders as necessary in order to facilitate appropriate decision-making at general shareholder meetings.
- 1.2.2 While ensuring the accuracy of content, companies should strive to send convening notices for general shareholder meetings early enough to give shareholders sufficient time to consider the agenda. During the period between the board approval of convening the general shareholder meeting and sending the convening notice, information included in the convening notice should be disclosed by electronic means such as through TDnet¹ or on the company's website.
- 1.2.3 The determination of the date of the general shareholder meeting and any associated dates should be made in consideration of facilitating sufficient constructive dialogue with shareholders and ensuring the accuracy of information necessary for such dialogue.
- 1.2.4 Bearing in mind the number of institutional and foreign shareholders, companies should take steps for the creation of an infrastructure allowing electronic voting, including the use of the Electronic Voting Platform, and the provision of English translations of the convening notices of general shareholder meeting.
- 1.2.5 In order to prepare for cases where institutional investors who hold shares in street name express an interest in advance of the general shareholder meeting in attending the general shareholder meeting or exercising voting rights,

¹ TDnet: The Tokyo Stock Exchange operates a real-time internet service (Timely Disclosure network) which distributes the information provided by listed companies on a timely basis in accordance with its listing rules.

companies should work with the trust bank (*shintaku ginko*) and/or custodial institutions to consider such possibility.

Principle 1.3 Basic Strategy for Capital Policy

Because capital policy may have a significant effect on shareholder returns, companies should explain their basic strategy with respect to their capital policy.

Principle 1.4 Cross-Shareholdings

When companies hold shares of other listed companies as cross-shareholdings², they should disclose their policy with respect to doing so, including their policies regarding the reduction of cross-shareholdings. In addition, the board should ~~examine the mid- to long-term economic rationale and future outlook of major cross-shareholdings on an annual basis, taking into consideration both associated risks and returns. The annual examination should result in the board's detailed explanation of the objective and rationale behind cross-shareholdings~~ annually assess whether or not to hold each individual cross-shareholding, specifically examining whether the purpose is appropriate and whether the benefits and risks from each holding cover the company's cost of capital. The results of this assessment should be disclosed.

Companies should establish and disclose specific standards with respect to the voting rights as to their cross-shareholdings, and vote in accordance with the standards.

Supplementary Principles

1.4.1 When cross-shareholders (i.e., shareholders who hold a company's shares for the purpose of cross-shareholding) indicate their intention to sell their shares, companies should not hinder the sale of the cross-held shares by, for instance, implying a possible reduction of business transactions.

² Cross-shareholding: There are cases where listed companies hold the shares of other listed companies for reasons other than pure investment purposes, for example, to strengthen business relationships. Cross-shareholdings here include not only mutual shareholdings but also unilateral ones.

1.4.2 Companies should not engage in transactions with cross-shareholders which may harm the interests of the companies or the common interests of their shareholders by, for instance, continuing the transactions without carefully examining the underlying economic rationale.

Principle 1.5 Anti-Takeover Measures

Anti-takeover measures must not have any objective associated with entrenchment of the management or the board. With respect to the adoption or implementation of anti-takeover measures, the board and *kansayaku*³ should carefully examine their necessity and rationale in light of their fiduciary responsibility to shareholders, ensure appropriate procedures, and provide sufficient explanation to shareholders.

Supplementary Principle

- 1.5.1 In case of a tender offer, companies should clearly explain the position of the board, including any counteroffers, and should not take measures that would frustrate shareholder rights to sell their shares in response to the tender offer.

Principle 1.6 Capital Policy that May Harm Shareholder Interests

With respect to a company's capital policy that results in the change of control or in significant dilution, including share offerings and management buyouts, the board and *kansayaku* should, in order not to unfairly harm the existing shareholders' interests, carefully examine the necessity and rationale from the perspective of their fiduciary responsibility to shareholders, should ensure appropriate procedures, and provide sufficient explanation to shareholders.

Principle 1.7 Related Party Transactions

When a company engages in transactions with its directors or major shareholders (i.e., related party transactions), in order to ensure that such transactions do not harm the interests of the company or the common interests of its shareholders and prevent any concerns with respect to such harm, the board should establish appropriate procedures beforehand in proportion to the importance and characteristics of the transaction. In addition to their use by the board in approving and monitoring such transactions, these procedures should be disclosed.

³ *Kansayaku*. See [Notes](#) to the General Principle 4.

Section 2: Appropriate Cooperation with Stakeholders Other Than Shareholders

General Principle 2

Companies should fully recognize that their sustainable growth and the creation of mid- to long-term corporate value are brought about as a result of the provision of resources and contributions made by a range of stakeholders, including employees, customers, business partners, creditors and local communities. As such, companies should endeavor to appropriately cooperate with these stakeholders.

The board and the management should exercise their leadership in establishing a corporate culture where the rights and positions of stakeholders are respected and sound business ethics are ensured.

Notes

Companies have a variety of important stakeholders besides shareholders. These stakeholders include internal parties such as employees and external parties such as customers, business partners and creditors. In addition, local communities form the foundation for the on-going business activities of companies. Companies should fully recognize that appropriate cooperation with these stakeholders is indispensable in achieving sustainable growth and increasing corporate value over the mid- to long-term. Given the recent and growing interest in social and environmental problems worldwide, taking positive and proactive measures toward ESG (environmental, social and governance) matters may also be included as part of this cooperation.

The appropriate actions of companies based on the recognition of their stakeholder responsibilities will benefit the entire economy and society, which will in turn contribute to producing further benefits to companies, thereby creating a virtuous cycle.

Principle 2.1 Business Principles as the Foundation of Corporate Value Creation Over the Mid- to Long-Term

Guided by their position concerning social responsibility, companies should undertake their businesses in order to create value for all stakeholders while increasing corporate value over the mid- to long-term. To this end, companies should draft and maintain business principles that will become the basis for such activities.

Principle 2.2 Code of Conduct

Companies should draft and implement a code of conduct for employees in order to express their values with respect to appropriate cooperation with and serving the interests of stakeholders and carrying out sound and ethical business activities. The board should be responsible for drafting and revising the code of conduct, and should ensure its compliance broadly across the organization, including the front line of domestic and global operations.

Supplementary Principle

2.2.1 The board should review regularly (or where appropriate) whether or not the code of conduct is being widely implemented. The review should focus on the substantive assessment of whether the company's corporate culture truly embraces the intent and spirit of the code of conduct, and not solely on the form of implementation and compliance.

Principle 2.3 Sustainability Issues, Including Social and Environmental Matters

Companies should take appropriate measures to address sustainability issues, including social and environmental matters.

Supplementary Principle

2.3.1 With the recognition that dealing with sustainability issues is an important element of risk management, the board should take appropriate actions to this end. Given the increasing demand and interest with respect to sustainability issues in recent years, the board should consider addressing these matters positively and proactively.

Principle 2.4 Ensuring Diversity, Including Active Participation of Women

Companies should recognize that the existence of diverse perspectives and values reflecting a variety of experiences, skills and characteristics is a strength that supports their sustainable growth. As such, companies should promote diversity of personnel, including the active participation of women.

Principle 2.5 Whistleblowing

Companies should establish an appropriate framework for whistleblowing such that employees can report illegal or inappropriate behavior, disclosures, or any other serious concerns without fear of suffering from disadvantageous treatment. Also, the framework should allow for an objective assessment and appropriate response to the reported issues, and the board should be responsible for both establishing this framework, and ensuring and monitoring its enforcement.

Supplementary Principle

2.5.1 As a part of establishing a framework for whistleblowing, companies should establish a point of contact that is independent of the management (for example, a panel consisting of outside directors⁴ and outside *kansayaku*⁵). In addition, rules should be established to secure the confidentiality of the information provider and prohibit any disadvantageous treatment.

⁴ Outside director: A director who satisfies certain requirements such as not holding specific positions, including the position of executive director, in the company or its subsidiaries (Article 2, Paragraph 15 of the Companies Act). Furthermore, matters such as not holding a specific position in the parent company or other subsidiaries and not having specific kinship ties with controlling shareholders will be also required for outside directors after the 2014 amendments to the Companies Act.

⁵ Outside *kansayaku*: A *kansayaku* who satisfies certain requirements such as not holding specific positions, including the position of director, in the company or its subsidiaries (Article 2, Paragraph 16 of the Companies Act). Furthermore, matters such as not holding a specific position in the parent company or other subsidiaries and not having specific kinship ties with controlling shareholders will be also required for outside *kansayaku* after the 2014 amendments to the Companies Act.

Principle 2.6 Roles of Corporate Pension Funds as Asset Owners

Because the management of corporate pension funds impacts stable asset formation for employees and companies' own financial standing, companies should take and disclose measures to improve human resources and operational practices, such as the recruitment or assignment of qualified persons, in order to increase the investment management expertise of corporate pension funds (including stewardship activities such as monitoring the asset managers of corporate pension funds), thus making sure that corporate pension funds perform their roles as asset owners. Companies should ensure that conflicts of interest which could arise between pension fund beneficiaries and companies are appropriately managed.

Section 3: Ensuring Appropriate Information Disclosure and Transparency

General Principle 3

Companies should appropriately make information disclosure in compliance with the relevant laws and regulations, but should also strive to actively provide information beyond that required by law. This includes both financial information, such as financial standing and operating results, and non-financial information, such as business strategies and business issues, risk and governance.

The board should recognize that disclosed information will serve as the basis for constructive dialogue with shareholders, and therefore ensure that such information, particularly non-financial information, is accurate, clear and useful.

Notes

Companies are legally required to disclose a wide range of information. The timely and appropriate disclosure of information in accordance with the relevant laws and regulations is essential for investor protection and securing market confidence. The board, *kansayaku*, the *kansayaku* board⁶ and external auditors all bear an important responsibility in this regard, starting with the establishment of an appropriate internal control system as to financial information.

Companies should actively strive to provide information other than what is required by laws and regulations.

It has been noted that while the quantitative part of financial statements of Japanese companies conform to a standard format and therefore excel with respect to comparability, qualitative and non-financial information is often boiler-plate and lacking in detail, therefore less valuable. The board should actively commit to ensure that disclosed information, including non-financial information, is as valuable and useful as possible.

Irrespective of whether the disclosed information is required by law, the appropriate provision of information is an effective means to develop a shared awareness and

⁶ *Kansayaku* board: See [Notes](#) to the General Principle 4.

understanding with shareholders and other stakeholders, in particular given that as outsiders they suffer from information asymmetry. Appropriate information disclosure will also contribute to constructive dialogue based on Japan's Stewardship Code.

Principle 3.1 Full Disclosure

In addition to making information disclosure in compliance with relevant laws and regulations, companies should disclose and proactively provide the information listed below (along with the disclosures specified by the principles of the Code) in order to enhance transparency and fairness in decision-making and ensure effective corporate governance:

- i) Company objectives (e.g., business principles), business strategies and business plans;
- ii) Basic views and guidelines on corporate governance based on each of the principles of the Code;
- iii) Board policies and procedures in determining the remuneration of the senior management and directors;
- iv) Board policies and procedures in the appointment/dismissal of the senior management and the nomination of directors and *kansayaku* candidates; and
- v) Explanations with respect to the individual appointments/dismissals and nominations based on iv).

Supplementary Principles

- 3.1.1 These disclosures, including disclosures in compliance with relevant laws and regulations, should add value for investors, and the board should ensure that information is not boiler-plate or lacking in detail.
- 3.1.2 Bearing in mind the number of foreign shareholders, companies should, to the extent reasonable, take steps for providing English language disclosures.

Principle 3.2 External Auditors

External auditors and companies should recognize the responsibility that external auditors owe toward shareholders and investors, and take appropriate steps to secure the proper execution of audits.

Supplementary Principles

3.2.1 The *kansayaku* board should, at minimum, ensure the following:

- i) Establish standards for the appropriate selection of external auditor candidates and proper evaluation of external auditors; and
- ii) Verify whether external auditors possess necessary independence and expertise to fulfill their responsibilities.

3.2.2 The board and the *kansayaku* board should, at minimum, ensure the following:

- i) Give adequate time to ensure high quality audits;
- ii) Ensure that external auditors have access, such as via interviews, to the senior management including the CEO and the CFO;
- iii) Ensure adequate coordination between external auditors and each of the *kansayaku* (including attendance at the *kansayaku* board meetings), the internal audit department and outside directors; and
- iv) Ensure that the company is constituted in the way that it can adequately respond to any misconduct, inadequacies or concerns identified by the external auditors.

Section 4: Responsibilities of the Board

General Principle 4

Given its fiduciary responsibility and accountability to shareholders, in order to promote sustainable corporate growth and the increase of corporate value over the mid- to long-term and enhance earnings power and capital efficiency, the board should appropriately fulfill its roles and responsibilities, including:

- (1) Setting the broad direction of corporate strategy;
- (2) Establishing an environment where appropriate risk-taking by the senior management is supported; and
- (3) Carrying out effective oversight of directors and the management (including *shikkoyaku*⁷ and so-called *shikkoyakuin*⁸) from an independent and objective standpoint.

Such roles and responsibilities should be equally and appropriately fulfilled regardless of the form of corporate organization – i.e., Company with *Kansayaku* Board (where a part of these roles and responsibilities are performed by *kansayaku* and the *kansayaku* board), Company with Three Committees (Nomination, Audit and Remuneration) or Company with Supervisory Committee.

Notes

Companies may choose one of three main forms of organizational structure under the Companies Act (Revised in 2014): Company with *Kansayaku* Board, Company with Three Committees (Nomination, Audit and Remuneration), or Company with Supervisory Committee. A Company with *Kansayaku* Board is a system unique to Japan

⁷ *Shikkoyaku*: According to the Companies Act, Companies with Three Committees (Nomination, Audit and Remuneration) must appoint one or more *shikkoyaku* from directors or non-directors by a resolution of the board and delegate business administration to *shikkoyaku*. Also, authority to make certain kinds of business decisions may be delegated to *shikkoyaku*.

⁸ *Shikkoyakuin*: There are cases where a Company with *Kansayaku* Board or a Company with Supervisory Committee creates positions with the title of “*shikkoyakuin*” for persons who are delegated by the board a certain range of discretion regarding business administration. Unlike *shikkoyaku* in Companies with Three Committees (Nomination, Audit and Remuneration), *shikkoyakuin* is not a statutory position.

in which certain governance functions are assumed by the board, *kansayaku* and the *kansayaku* board. Under this system, *kansayaku* audit the performance of duties by directors and the management and have investigation power by law. Also, to secure both independence and high-level information gathering power, not less than half of *kansayaku*, as appointed at the general shareholder meeting, must be outside *kansayaku*, and at least one full-time *kansayaku* must also be appointed. The latter two forms of organizational structure are similar to companies in other countries where committees are established under the board and assigned certain responsibilities with the aim of strengthening monitoring functions. Irrespective of which form of organizational structure is adopted, what is important is that the various institutions within the company effectively and fully execute their responsibilities through creativity and ingenuity.

One of the major objectives of establishing the Code is to promote transparent, fair, timely and decisive decision-making by Japanese companies. The possibility cannot be ruled out that, due to changes in the external environment or other factors, a decision made by a company ultimately results in losses for the company. In such a circumstance, the reasonableness of the decision-making process at the time of the decision is generally considered an important factor in determining whether or not the management and directors should owe personal liability for damages. The Code includes principles and practices that are expected to contribute to such a reasonable decision-making process, and promote transparency, fairness, timeliness and decisiveness as well.

Principle 4.1 Roles and Responsibilities of the Board (1)

The board should view the establishment of corporate goals (business principles, etc.) and the setting of strategic direction as one major aspect of its roles and responsibilities. It should engage in constructive discussion with respect to specific business strategies and business plans, and ensure that major operational decisions are based on the company's strategic direction.

Supplementary Principles

4.1.1 The board should clearly specify its own decisions as well as both the scope and content of the matters delegated to the management, and disclose a brief summary thereof.

- 4.1.2 Recognizing that a mid-term business plan (*chuuiki keiei keikaku*) is a commitment to shareholders, the board and the senior management should do their best to achieve the plan. Should the company fail to deliver on its mid-term business plan, the reasons underlying the failure of achievement as well as the company's actions should be fully analyzed, an appropriate explanation should be given to shareholders, and analytic findings should be reflected in a plan for the ensuing years.
- 4.1.3 Based on the company objectives (business principles, etc.) and specific business strategies, the board should proactively engage in the appropriate oversight establishment and implementation of a succession planning for the CEO and other top executives and appropriately oversee the systematic development of succession candidates, deploying sufficient time and resources.

Principle 4.2 Roles and Responsibilities of the Board (2)

The board should view the establishment of an environment that supports appropriate risk-taking by the senior management as a major aspect of its roles and responsibilities. It should welcome proposals from the management based on healthy entrepreneurship, fully examine such proposals from an independent and objective standpoint with the aim of securing accountability, and support timely and decisive decision-making by the senior management when approved plans are implemented.

Also, the remuneration of the management should include incentives such that it reflects mid- to long-term business results and potential risks, as well as promotes healthy entrepreneurship.

Supplementary Principle

- 4.2.1 ~~In order for~~The board should design management remuneration ~~to~~systems such that they operate as a healthy incentive ~~for~~to generate sustainable growth, and determine actual remuneration amounts appropriately through objective and transparent procedures. ~~†~~The proportion of management remuneration linked to mid- to long-term results and the balance of cash and stock should be set appropriately.

Principle 4.3 Roles and Responsibilities of the Board (3)

The board should view the effective oversight of the management and directors from an independent and objective standpoint as a major aspect of its roles and responsibilities. It should appropriately evaluate company performance and reflect the evaluation in its assessment of the senior management.

In addition, the board should engage in oversight activities in order to ensure timely and accurate information disclosure, and should establish appropriate internal control and risk management systems.

Also, the board should appropriately deal with any conflict of interests that may arise between the company and its related parties, including the management and controlling shareholders.

Supplementary Principles

4.3.1 The board should ensure that the appointment and dismissal of the senior management are based on highly transparent and fair procedures ~~and reflect the results of company performance~~ via an appropriate evaluation of the company's business results.

4.3.2 Because the appointment/dismissal of the CEO is the most important strategic decision for a company, the board should appoint a qualified CEO through objective, timely, and transparent procedures, deploying sufficient time and resources.

4.3.3 The board should establish objective, timely, and transparent procedures such that a CEO is dismissed when it is determined, via an appropriate evaluation of the company's business results, that the CEO is not adequately fulfilling the CEO's responsibilities.

4.3.24 The establishment of effective internal control and proactive risk management systems for compliance and financial reporting has the potential of supporting sound risk-taking. The board should place priority on the appropriate establishment of such systems and the oversight of whether they effectively operate, and should not limit itself to the examination of compliance with respect to specific business operations.

Principle 4.4 Roles and Responsibilities of *Kansayaku* and the *Kansayaku* Board

Kansayaku and the *kansayaku* board should bear in mind their fiduciary responsibilities to shareholders and make decisions from an independent and objective standpoint when executing their roles and responsibilities including the audit of the performance of directors' duties, appointment and dismissal of external auditors and the determination of auditor remuneration.

Although so-called “defensive functions,” such as business and accounting audits, are part of the roles and responsibilities expected of *kansayaku* and the *kansayaku* board, in order to fully perform their duties, it would not be appropriate for *kansayaku* and the *kansayaku* board to interpret the scope of their function too narrowly, and they should positively and proactively exercise their rights and express their views at board meetings and to the management.

Supplementary Principle

4.4.1 Given that not less than half of the *kansayaku* board must be composed of outside *kansayaku* and that at least one full-time *kansayaku* must be appointed in accordance with the Companies Act, the *kansayaku* board should, from the perspective of fully executing its roles and responsibilities, increase its effectiveness through an organizational combination of the independence of the former and the information gathering power of the latter. In addition, *kansayaku* or the *kansayaku* board should secure cooperation with outside directors so that such directors can strengthen their capacity to collect information without having their independence jeopardized.

Principle 4.5 Fiduciary Responsibilities of Directors and *Kansayaku*

With due attention to their fiduciary responsibilities to shareholders, the directors, *kansayaku* and the management of companies should secure the appropriate cooperation with stakeholders and act in the interest of the company and the common interests of its shareholders.

Principle 4.6 Business Execution and Oversight of the Management

In order to ensure effective, independent and objective oversight of the management by the board, companies should consider utilizing directors who are neither involved in business execution nor have close ties with the management.

Principle 4.7 Roles and Responsibilities of Independent Directors

Companies should make effective use of independent directors⁹, taking into consideration the expectations listed below with respect to their roles and responsibilities:

- i) Provision of advice on business policies and business improvement based on their knowledge and experience with the aim to promote sustainable corporate growth and increase corporate value over the mid- to long-term;
- ii) Monitoring of the management through important decision-making at the board including the appointment and dismissal of the senior management;
- iii) Monitoring of conflicts of interest between the company and the management or controlling shareholders; and
- iv) Appropriately representing the views of minority shareholders and other stakeholders in the boardroom from a standpoint independent of the management and controlling shareholders.

Principle 4.8 Effective Use of Independent Directors

Independent directors should fulfill their roles and responsibilities with the aim of contributing to sustainable growth of companies and increasing corporate value over the mid- to long-term. Companies should therefore appoint at least two independent directors that sufficiently have such qualities.

Irrespective of the above, if a company ~~in its own judgement~~ believes it needs to appoint at least one-third of directors as independent directors based on a broad

⁹ Independent director: The listing rules of securities exchanges provide that the outside directors, as defined in the Companies Act, are independent directors where they satisfy independence criteria of securities exchanges and the company determines that they do not have the possibility of conflicts of interest with its shareholders.

consideration of factors such as the industry, company size, business characteristics, organizational structure and circumstances surrounding the company, it should ~~disclose a roadmap for doing so~~ appoint a sufficient number of independent directors.

Supplementary Principles

- 4.8.1 In order to actively contribute to discussions at the board, independent directors should endeavor to exchange information and develop a shared awareness among themselves from an independent and objective standpoint. Regular meetings consisting solely of independent directors (executive sessions) would be one way of achieving this.
- 4.8.2 Independent directors should endeavor to establish a framework for communicating with the management and for cooperating with *kansayaku* or the *kansayaku* board by, for example, appointing the lead independent director from among themselves.

Principle 4.9 Independence Standards and Qualification for Independent Directors

Boards should establish and disclose independence standards aimed at securing effective independence of independent directors, taking into consideration the independence criteria set by securities exchanges. The board should endeavor to select independent director candidates who are expected to contribute to frank, active and constructive discussions at board meetings.

Principle 4.10 Use of Optional Approach

In adopting the most appropriate organizational structure (as stipulated by the Companies Act) that is suitable for a company's specific characteristics, companies should employ optional approaches, as necessary, to further enhance governance functions.

Supplementary Principle

- 4.10.1 If the organizational structure of a company is either Company with *Kansayaku* Board or Company with Supervisory Committee and independent directors do not compose a majority of the board, in order to strengthen the independence,

objectivity and accountability of board functions on the matters of nomination and remuneration of the senior management and directors, the company should seek appropriate involvement and advice from independent directors in the examination of such important matters as nominations and remuneration by, ~~for example,~~ establishing ~~optional~~independent advisory committees under the board, such as an optional¹⁰ nomination committee and an optional remuneration committee, to which independent directors make significant contributions.

Principle 4.11 Preconditions for Board and *Kansayaku* Board Effectiveness

The board should be well balanced in knowledge, experience and skills in order to fulfill its roles and responsibilities, and it should be constituted in a manner to achieve both diversity, including gender and international experience, and appropriate size. In addition, persons with appropriate experience and skills as well as necessary knowledge on finance, accounting, and the law should be appointed as *kansayaku*. In particular, at least one person who has ~~appropriate~~sufficient expertise on finance and accounting should be appointed as *kansayaku*.

The board should endeavor to improve its function by analyzing and evaluating effectiveness of the board as a whole.

Supplementary Principles

4.11.1 The board should have a view on the appropriate balance between knowledge, experience and skills of the board as a whole, and also on diversity and appropriate board size. Consistent with its view, the board should establish policies and procedures for nominating directors and disclose them along with its view.

4.11.2 Outside directors, outside *kansayaku*, and other directors and *kansayaku* should devote sufficient time and effort required to appropriately fulfill their respective roles and responsibilities. Therefore, where directors and *kansayaku* also serve as directors, *kansayaku* or the management at other companies, such positions

¹⁰ If a company is either a Company with *Kansayaku* Board or Company with Supervisory Committee, the company is not required to establish a nomination committee or a remuneration committee by the Companies Act. However, the company may establish such committees on its own initiative.

should be limited to a reasonable number and disclosed each year.

- 4.11.3 Each year the board should analyze and evaluate its effectiveness as a whole, taking into consideration the relevant matters, including the self-evaluations of each director. A summary of the results should be disclosed.

Principle 4.12 Active Board Deliberations

The board should endeavor to foster a climate where free, open and constructive discussions and exchanges of views take place, including the raising of concerns by outside directors.

Supplementary Principle

- 4.12.1 The board should ensure the following in relation to the operation of board meetings and should attempt to make deliberations active:
- i) Materials for board meetings are distributed sufficiently in advance of the meeting date;
 - ii) In addition to board materials and as necessary, sufficient information is provided to directors by the company (where appropriate, the information should be organized and/or analyzed to promote easy understanding);
 - iii) The schedule of board meetings for the current year and anticipated agenda items are determined in advance;
 - iv) The number of agenda items and the frequency of board meetings are set appropriately; and
 - v) Sufficient time for deliberations.

Principle 4.13 Information Gathering and Support Structure

In order to fulfill their roles and responsibilities, directors and *kansayaku* should proactively collect information, and as necessary, request the company to provide them

with additional information.

Also, companies should establish a support structure for directors and *kansayaku*, including providing sufficient staff.

The board and the *kansayaku* board should verify whether information requested by directors and *kansayaku* is provided smoothly.

Supplementary Principles

4.13.1 Directors, including outside directors, should request the company to provide them with additional information, where deemed necessary from the perspective of contributing to transparent, fair, timely and decisive decision-making. In addition, *kansayaku*, including outside *kansayaku*, should collect information appropriately, including the use of their statutory investigation power.

4.13.2 Directors and *kansayaku* should consider consulting with external specialists at company expense, where they deem it necessary.

4.13.3 Companies should ensure coordination between the internal audit department, directors and *kansayaku*. In addition, companies should take measures to adequately provide necessary information to outside directors and outside *kansayaku*. One example would be the appointment of an individual who is responsible for communicating and handling requests within the company such that the requests for information about the company by outside directors and outside *kansayaku* are appropriately processed.

Principle 4.14 Director and *Kansayaku* Training

New and incumbent directors and *kansayaku* should deepen their understanding of their roles and responsibilities as a critical governance body at a company, and should endeavor to acquire and update necessary knowledge and skills. Accordingly, companies should provide and arrange training opportunities suitable to each director and *kansayaku* along with financial support for associated expenses. The board should verify whether such opportunities and support are appropriately provided.

Supplementary Principles

4.14.1 Directors and *kansayaku*, including outside directors and outside *kansayaku*,

should be given the opportunity when assuming their position to acquire necessary knowledge on the company's business, finances, organization and other matters, and fully understand the roles and responsibilities, including legal liabilities, expected of them. Incumbent directors should also be given a continuing opportunity to renew and update such knowledge as necessary.

4.14.2 Companies should disclose their training policy for directors and *kansayaku*.

Section 5: Dialogue with Shareholders

General Principle 5

In order to contribute to sustainable growth and the increase of corporate value over the mid- to long-term, companies should engage in constructive dialogue with shareholders even outside the general shareholder meeting.

During such dialogue, senior management and directors, including outside directors, should listen to the views of shareholders and pay due attention to their interests and concerns, clearly explain business policies to shareholders in an understandable manner so as to gain their support, and work for developing a balanced understanding of the positions of shareholders and other stakeholders and acting accordingly.

Notes

With the establishment of Japan's Stewardship Code, institutional investors are encouraged to engage in purposeful dialogue (engagement) based on the in-depth knowledge of investee companies and their business environment.

Regularly engaging in dialogue with shareholders to gain their understanding of specific business strategies and business plans and taking appropriate action when there are concerns are extraordinarily useful for companies to strengthen the foundations of management legitimacy and support their efforts to generate sustainable growth. Although the management and directors have opportunities to interact and exchange views with employees, business partners and financial institutions on a daily basis, these stakeholders are all creditors. In contrast, the management and directors typically have limited interactions with shareholders. If the senior management and directors give due attention to the views of shareholders through dialogue, they can absorb views and analyses of business management from the perspective of capital providers. Dialogue with shareholders should also inspire healthy entrepreneurship in the management and directors and thereby contribute to sustainable corporate growth.

Principle 5.1 Policy for Constructive Dialogue with Shareholders

Companies should, positively and to the extent reasonable, respond to the requests from shareholders to engage in dialogue (management meetings) so as to support sustainable growth and increase corporate value over the mid- to long-term. The board should establish, approve and disclose policies concerning the measures and organizational structures aimed at promoting constructive dialogue with shareholders.

Supplementary Principles

- 5.1.1 Taking the requests and interests of shareholders into consideration, to the extent reasonable, the senior management and directors, including outside directors, should have a basic position to engage in dialogue (management meetings) with shareholders.
- 5.1.2 At minimum, policies for promoting constructive dialogue with shareholders should include the following:
- i) Appointing a member of the management or a director who is responsible for overseeing and ensuring that constructive dialogue takes place, including the matters stated in items ii) to v) below;
 - ii) Measures to ensure positive cooperation between internal departments such as investor relations, corporate planning, general affairs, corporate finance, accounting and legal affairs with the aim of supporting dialogue;
 - iii) Measures to promote opportunities for dialogue aside from individual meetings (e.g., general investor meetings and other IR activities);
 - iv) Measures to appropriately and effectively relay shareholder views and concerns learned through dialogue to the senior management and the board; and
 - v) Measures to control insider information when engaging in dialogue.

- 5.1.3 Companies should endeavor to identify their shareholder ownership structure as necessary, and it is desirable for shareholders to cooperate as much as possible in this process.

Principle 5.2 Establishing and Disclosing Business Strategies and Business Plans

When establishing and disclosing business strategies and business plans, companies should articulate their earnings plans and capital policies, and present targets for profitability and capital efficiency after accurately identifying the company's cost of capital. Also, companies should provide explanations that are clear and logical to shareholders with respect to the allocation of management resources, such as reviewing their business portfolio and investments in fixed assets, R&D, and human resources, and specific measures that will be taken in order to achieve their plans and targets.

**Revision of the Corporate Governance Code and
Establishment of Guidelines for Investor and Company Engagement**

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

March 26, 2018

I . Introduction

A degree of progress has been seen in corporate governance reform due to various measures including the establishment of the Stewardship Code in 2014 (revised in 2017) and the Corporate Governance Code in 2015. On the other hand, looking at the current situation, a number of issues still exist, such as the lack of decisive decisions by management at many companies. It has also been pointed out that engagement between investors and companies is often merely a formality, and there are just a limited number of cases where engagement has resulted in fruitful insights for companies.

In light of these issues, since October 2017 the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code (hereafter, the "Council") has examined the progress of Japan's corporate governance reform, and has made proposals to revise the Corporate Governance Code in order to deepen and make more substantive this reform (cf. Appendix 1 for the specific revision proposal; hereafter, the "Code Revision Draft"). In addition, in order to encourage institutional investors and companies to effectively implement the Stewardship Code and the Corporate Governance Code on a "comply or explain" basis, the Council has proposed the drafting of Guidelines for Investor and Company Engagement (hereafter, the "Engagement Guidelines") that provide agenda items for engagement. It is expected that institutional investors and companies will engage each other with respect to these agenda items, along with the Code revision (cf. Appendix 2 for the specific proposal).

II. Ideas Underlying the Revision of the Code and the Establishment of the Engagement Guidelines

The basic ideas underlying this proposal for the Code Revision Draft and the Engagement Guidelines Draft are as follows.

1. Management Decisions in Response to Changes in the Business Environment

The aim of corporate governance reform is to promote sustainable growth and increase corporate value over the mid- to long-term by encouraging decisive decisions by management. While there are some Japanese companies who have undertaken corporate governance reform to increase their corporate value, it has been pointed out that many companies are not making management decisions decisively in response to changes in the business environment, an issue that needs to be taken very seriously. For example, it has been pointed out that the reviewing of business portfolios is not necessarily sufficient at Japanese companies, because management still does not adequately recognize a company's cost of capital.

In light of these issues, it is necessary to clarify that decisive management decisions, including reviewing business portfolios, are important, and management should accurately identify a company's cost of capital in order to make such management decisions.

2. Investment Strategy and Financial Management Policy

Strategic and systematic investments in fixed assets, R&D, and human resources are important for companies to generate sustainable growth and increase corporate value over the mid- to long-term. In making such investments, it is also important to conduct appropriate financial management which is consistent with investment strategies and recognizes a company's cost of capital.

3. CEO Appointment/Dismissal and Responsibilities of the Board

CEO Appointment/Dismissal

The CEO plays a central role in management, and CEO appointment/dismissal is the most important strategic decision for a company.¹¹

On the other hand, it has been pointed out that initiatives with respect to the development and appointment of a CEO have been insufficient at many companies, and it is necessary to establish objective, timely, and transparent procedures to this end. For example, there are companies that still have not established policies for CEO appointment/dismissal, and there are few companies in which the board engages in sufficient oversight of succession plans. Furthermore, although increasing number of companies have recently established a nomination committee, it is important to further promote the establishment and use of nomination committees in order to strengthen the independence and objectivity of the CEO appointment/dismissal process.

Responsibilities of the Board

The board has the responsibility to support management including the CEO, and it is necessary for the board as a whole to possess appropriate knowledge, experience, and skills.

In addition, the ratio of female officers at Japanese listed companies is currently only 3.7%, and it is important to ensure sufficient diversity, including gender and international experience, in order for the board to sufficiently fulfill its

¹¹ CEO appointment/dismissal has been the subject of discussion by the Council; cf. the Opinion Statement entitled "Corporate Boards Seeking Sustainable Corporate Growth and Increased Corporate Value over the Mid- to Long-Term," February 2016.

responsibilities.

4. Cross-Shareholdings

While cross-shareholdings have decreased recently, the decrease by non-financial corporations is modest, and the ratio of voting rights accounted for by cross-shareholdings remains high.

It has been pointed out that cross-shareholdings are meaningful in promoting strategic partnerships. However, it has also been pointed out that the presence of shareholders who are expected to support company management could lead to a lack of management discipline, and that cross-shareholdings are risk assets on company balance sheets that are not proactively used and therefore inefficient in terms of capital management.

Considering these circumstances, it is important for investors and companies to deepen their engagement on cross-shareholdings. Companies need to assess whether or not to hold each individual cross-shareholding, and clearly disclose and explain the results of this assessment after specifically examining the purpose, benefits, and risks of each holding. In addition, it is important to clearly disclose policies with respect to cross-shareholdings, including the policies regarding the reduction of cross-shareholdings.

The importance of discipline at companies whose shares are being held as cross-shareholdings has also been pointed out, and this issue is addressed in the revision of the Code.

5. Asset Owners

Asset owners are positioned closest to the ultimate beneficiaries and are able to encourage and monitor asset managers that are the direct counterparties in engagement with companies. The role of asset owners is thus extremely important to deepen corporate governance reform and promote the smooth functioning of the investment chain.

Among asset owners, while there have been some public pension funds that have instructed asset managers to engage in effective stewardship activities in response to the revision of the Stewardship Code in May of last year, corporate pension funds' actions have not necessarily been adequate. It has been pointed out that corporate pension funds in general have not shown interest in stewardship activities, and that few corporate pension funds actually conduct such activities, with only nine corporate pension funds having become signatories of the Stewardship Code. In addition, it has been pointed out that corporate pension funds lack human resources – in terms of both quality and quantity – for investment management including

stewardship activities.

Although these are issues that should primarily be addressed by corporate pension funds themselves, plan sponsor companies should fully recognize that the management of corporate pension funds impacts stable asset formation for employees and companies' own financial standing and take measures on their own to improve human resources and operational practices, thus making sure that corporate pension funds perform their roles as asset owners. Although corporate pension funds in Japan exceed 10,000 in number and are diverse in structure and size, it is expected that these actions will contribute to increasing the investment management expertise of corporate pension funds and the number of Stewardship Code signatories, and promote effective stewardship activities.

III. Closing Remarks

The Council expects that in accordance with the proposed drafts the Tokyo Stock Exchange will promptly revise the Corporate Governance Code and the Financial Services Agency will promptly issue the Engagement Guidelines.

Guidelines for Investor and Company Engagement

(Draft)

Financial Services Agency

March 26, 2018

Guidelines for Investor and Company Engagement

The Guidelines herein provide agenda items for engagement that institutional investors and companies are expected to focus on based on the Stewardship Code and the Corporate Governance Code, in recognition of the corporate governance issues prevalent at this time. Through constructive engagement with institutional investors, companies are expected to generate sustainable growth and increase corporate value over the mid- to long-term based on their own business principles¹, which will eventually lead to the growth of the Japanese economy as a whole and stable asset formation for the Japanese people.

The Guidelines are intended to be a supplemental document to the Stewardship Code and the Corporate Governance Code. Although the intention is not to require institutional investors and companies to “comply or explain” with respect to the Guidelines themselves, the Guidelines are intended to encourage institutional investors and companies to implement both Codes effectively on a “comply or explain” basis². Companies are expected to consider the contents of the Guidelines when they comply with a principle of the Corporate Governance Code, including principles calling for disclosure, or, if not, explain the reasons why they are not doing so.

Because corporate governance issues and company priorities are diverse, it is not appropriate to use the Guidelines’ agenda items as a mechanical checklist, and it is important to have effective engagement between investors and companies that takes into consideration each company’s specific circumstances³.

1. Management Decisions in Response to Changes in the Business Environment

- 1.1 Are specific business strategies and business plans established and disclosed to generate sustainable growth and increase corporate value over the mid- to long-term? Are these business strategies and business plans consistent with the company’s business principles?
- 1.2 Does management accurately identify the company’s cost of capital, reflecting risks associated with the business in an appropriate manner? Does management manage the business with a recognition of the company’s cost of capital by setting targets on profitability and capital efficiency to generate sustainable growth and increase corporate value over the mid- to long-term? Does management clearly explain why they decided upon such targets? Does the company achieve returns which cover the cost of capital on a mid- to long-term basis?

¹ Depending upon the company, “business principles” may be described as a “vision,” “mission,” or “philosophy”.

² In order to enhance constructive engagement between institutional investors and companies, even when a company complies with a principle, it is beneficial for the company to proactively explain its specific implementation activities.

³ There are many cases where a company is managed as part of a corporate group, and the Guidelines have been established taking such companies into consideration. In such cases, it is expected that investors will view the company in light of its corporate group status.

- 1.3 Does management understand the business environment and business-related risks appropriately and make decisions decisively, such as restructuring the company's business portfolio, including investment in new businesses and exit from or sale of existing businesses, based on the company's business strategies and business plans? Is a policy on reviewing a business portfolio clearly established, and is the review process effective?

2. Investment Strategy and Financial Management Policy

- 2.1 Are investments in fixed assets, R&D, and human resources to generate sustainable growth and increase corporate value over the mid- to long-term carried out strategically and systematically using the company's resources and from the standpoint of generating returns which cover the company's cost of capital on a mid-to long- term basis?
- 2.2 Is financial management policy (including capital structure decisions and use of cash on hand in recognition of the company's cost of capital) established and managed appropriately based on the company's business and investment strategies?

3. CEO Appointment/Dismissal and Responsibilities of the Board

CEO Appointment/Dismissal and Development

- 3.1 Is there an established policy on CEO qualifications in order to appoint a CEO who can make decisions decisively to generate sustainable growth and increase corporate value over the mid-to long-term?
- 3.2 Is a qualified CEO appointed through objective, timely, and transparent procedures, deploying sufficient time and resources? In order to make these procedures effective, is an independent nomination committee actively involved?
- 3.3 Is a CEO succession plan appropriately established and implemented, and are CEO candidates developed or, if necessary, selected from outside the company, systematically deploying sufficient time and resources?
- 3.4 Are objective, timely, and transparent procedures established such that a CEO is dismissed when it is determined, via an appropriate evaluation of the company's business results, that the CEO is not adequately fulfilling the CEO's responsibilities?

Determination of Management Remuneration

- 3.5 Are objective and transparent procedures established to design management remuneration systems such that they operate as a healthy incentive to generate sustainable growth and increase corporate value over the mid- to long-term and to determine actual remuneration amounts appropriately? In order to make these procedures effective, is an independent remuneration committee actively involved? Is the appropriateness of the remuneration system and of the actual remuneration amount clearly explained?

Responsibilities of the Board

- 3.6 In order to generate sustainable growth and increase corporate value over the mid- to long-term, is the board of directors constituted in a manner such that it is equipped with appropriate knowledge, experience, and skills as a whole and ensures diversity, including gender and international experience? Are there women appointed as directors?
- 3.7 Is evaluation of the board's effectiveness as to whether the board fulfills its roles and responsibilities implemented appropriately, and are the evaluation results, including issues identified through such evaluation, clearly disclosed and explained?

Appointment of Independent Directors and Their Responsibilities

- 3.8 Is a sufficient number of qualified independent directors appointed? Do the independent directors possess the necessary knowledge to effectively contribute to sustainable growth and increasing corporate value over the mid- to long-term, including knowledge of finance, such as capital efficiency, and understanding of relevant laws and regulations?
Are appropriate actions taken for the reappointment or retirement of independent directors, taking into consideration the issues and changes facing the company?
- 3.9 Do independent directors recognize their roles and responsibilities, and provide advice and monitor management appropriately in response to business issues?

Appointment of *Kansayaku*⁴ and Their Responsibilities

- 3.10 Are persons with appropriate experience and skills as well as necessary knowledge on finance, accounting, and the law appointed as *kansayaku*?
- 3.11 Do *kansayaku* conduct business audits appropriately and act effectively to secure proper accounting audits? Is a sufficient support structure for *kansayaku* established and appropriate coordination between *kansayaku* and the internal audit department ensured?

⁴ The contents of this section are also intended to apply to Audit Committee Members of Companies with Three Committees and Supervisory Committee Members of Companies with Supervisory Committee. Companies may choose one of three main forms of organizational structure under the Companies Act (Revised in 2014): Company with *Kansayaku* Board, Company with Three Committees (Nomination, Audit and Remuneration), or Company with Supervisory Committee. A Company with *Kansayaku* Board is a system unique to Japan in which certain governance functions are assumed by the board, *kansayaku*, and the *kansayaku* board. Under this system, *kansayaku* audit the performance of duties by directors and the management and have investigation power by law (See [Notes](#) to the General Principle 4 of Japan's Corporate Governance Code).

4. Cross-Shareholdings

Assessment of Cross-Shareholdings

4.1 Does the company clearly explain the purpose of each cross-shareholding^{5,6} and the status of its cross-shareholdings, including any changes in its cross-shareholdings?

Does the board assess whether or not to hold each individual cross-shareholding, specifically examining whether the purpose is appropriate and whether the benefits and risks from each holding cover the company's cost of capital? Does the company appropriately make decisions based on such assessment? Does the company clearly disclose and explain the results of this assessment?

Has the company established appropriate standards that are clearly disclosed with respect to the voting rights as to cross-shareholdings? Does the company vote appropriately in accordance with the standards?

4.2 As part of its cross-shareholding policy disclosure, does the company make clear its policy regarding the reduction of cross-shareholdings, and take appropriate actions in accordance with the policy?

Relations with Cross-Shareholders

4.3 When cross-shareholders (i.e., shareholders who hold a company's shares for the purpose of cross-shareholding) indicate their intention to sell their shares, does the company hinder the sale of the cross-held shares by, for instance, implying possible reduction of business transactions?

4.4 Does the company engage in transactions with cross-shareholders which may harm the interests of the company or the common interests of their shareholders by, for instance, continuing the transactions without carefully examining the underlying economic rationale?

5. Asset Owners

5.1 As a pension fund sponsor, does the company take measures to improve human resources and operational practices, such as recruitment or assignment of qualified persons (including hiring outside experts), in order to increase the investment management expertise of corporate pension funds (including stewardship activities such as monitoring the asset managers of corporate pension funds), thus making sure that corporate pension funds perform their roles as asset owners?⁷ Are these measures clearly disclosed and explained?

⁵ There are cases where listed companies hold the shares of other listed companies for reasons other than pure investment purposes, for example, to strengthen business relationships. Cross-shareholdings here include not only mutual shareholdings but also unilateral ones.

⁶ Cross-shareholdings include shares that are not directly held by a company but in practice are under the company's control.

⁷ During engagements, investors and companies need to be careful to appropriately manage conflicts of interest which could arise between plan sponsor companies and pension fund beneficiaries as a result of these activities.