27th Meeting of the Council of Experts Concerning the Follow-up of Japan’s Stewardship Code and Japan’s Corporate Governance Code

Material 4

Provisional translation

Reference Materials for the 27th Meetng of Council

May 16, 2022

金融庁
Financial Services Agency, the Japanese Government

Contents

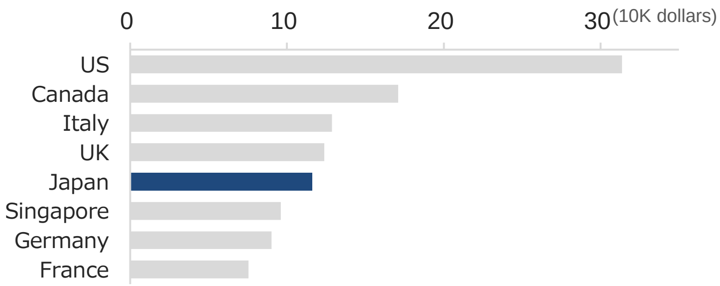
Remuneration levels of and skill held by outside directors in major countries

From "Corporate Governance: Is it Really So? 2 (tentative)," by Shoichi Tsumuraya

- The average remuneration of outside directors in Japanese companies is not necessarily low compared to other countries.
- The percentage of directors of Japanese companies possessing key skills is generally lower than in major countries, with a particularly large gap in finance and accounting skills compared to major countries.
- In addition, the disclosure of the activities of the nomination and remuneration committee is often boilerplate (note), which raises the question of whether outside directors are doing their jobs commensurate with their remuneration.

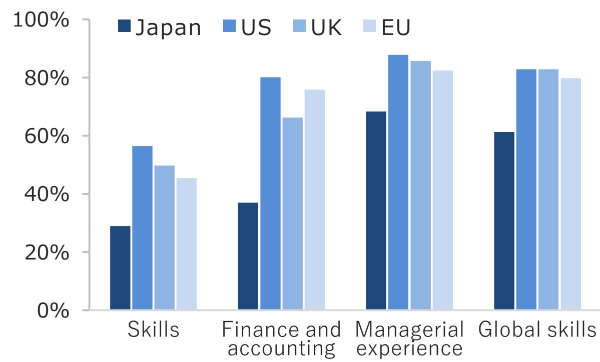
(Note) For example, "Under the board, the committee deliberates on and reports on proposals for consultation," "the committee decides on proposals for the election and dismissal of directors," or "the committee decides on policies and details regarding individual remuneration received by directors and executive officers," and other such statements that would not look out of place if reproduced in another company's disclosure materials are judged to be boilerplate. Note, that although the surveyors alignment on the criteria was performed from time to time, arbitrariness could not be completely eliminated in the classification process.

Remuneration of non-executive directors in major countries



(Note) The survey covers the major index constituents in each country, and the specific number of companies is unknown
(Source) Created by Tsumuraya members from Spencer Stuart's "Boards Around the World"

Percentage of directors with skills

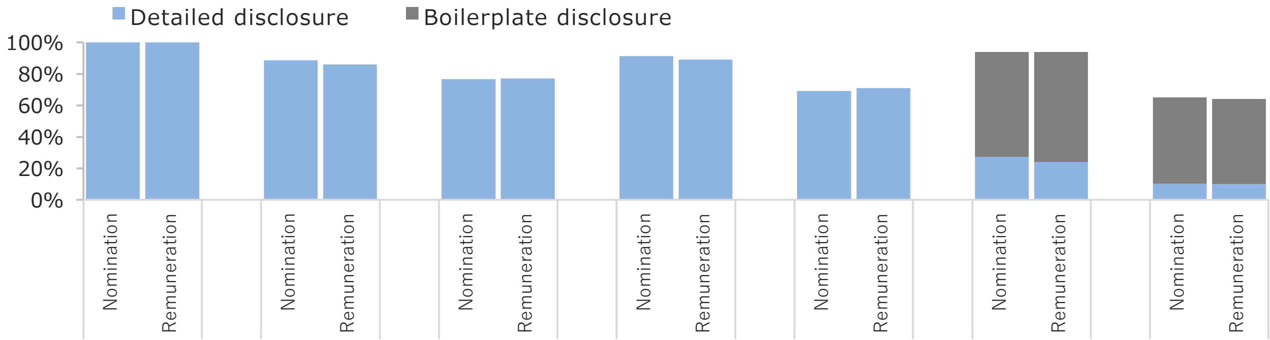


[Method of investigation and preparation]
We surveyed the annual reports (or integrated reports) of each company as of 2019, covering companies disclosing a skills matrix in each country.

[Japan] Of the 1,212 TSE 1st section companies with at least 3 outside directors, 93 disclose the skills of both inside and outside directors.
[US] 26 companies out of the Dow 30
[UK] 17 of the top 30 companies in the FTSE 100 by market capitalization
[Europe] 16 companies out of the Euro STOXX 50 (excluding non-English disclosing companies)

(Source) Tsumuraya (2021) Chart 1

Disclosure regarding the activities of the nomination committee and remuneration committee



[Survey sample and survey data from US companies]
Proxies for 65 NYSE-listed companies and 106 NASDAQ-listed companies (excluding mutual funds, REITs, etc.) for which data were available and for which Dow 30 companies and all NYSE and NASDAQ-listed companies were compressed to 1/20th in accordance with their market capitalization.

[Survey sample and survey data from Japanese companies]
Corporate governance report and integrated report of Nikkei 225 companies

(Source) Created by Tsumuraya members

Contents

Interviews with companies: working level questions

- Interviews at the working level (board secretariat, etc.) were conducted based on the following questions.

I. Your company's corporate governance reform initiatives to date, and an evaluation of the results of these initiatives (achievement of aggressive governance, sustainable growth of the company, and increase in corporate value).

1. Main initiatives and evaluation of results
   - (1) Efforts made prior to the Corporate Governance Code
   - (2) Efforts made in response to the Corporate Governance Code
   - (3) Efforts being made, or planned to be made, in response to the re-revision of the Corporate Governance Code (June 2021)

   * In considering corporate governance reform efforts and results, it may be helpful to consider, for example, the items stated in the appendix, but it is not necessary to respond in accordance with the appendix. We would appreciate it if your company could indicate the priorities of your initiatives, <u>starting with those that you consider to be of the highest priority</u>, including why you have taken such initiatives. You could also address viewpoints not stated in the appendix.

   * Regarding the evaluation of results, could you indicate using <u>specific cases as examples</u> , 1) whether the expected results have been achieved and 2) based on 1), how you intend to address it in the future?

2. The Corporate Governance Code that fall under following items
   - (1) Items that are difficult to implement immediately, although they are desired to be implemented
   - (2) Low priority items
   - (3) Items for which we do not feel the need, or for which we do not perceive much effect on improving corporate value compared to the cost (time and effort) required to implement the initiatives

II. (Based on I.) What is your assessment of the government's corporate governance reform efforts?
What elements of governance (aggressive governance) are necessary to improve corporate value over the medium to long term ?

Interviews with companies: working level questions (appendix)

Examples of corporate governance reform initiatives

[Fulfillment of functions of the board]

Initiatives stated below regarding the fulfillment of the functions of the board, and does each initiative have an impact on management actions, managerial awareness, and corporate value?

- ○ Discussion of management strategies and plans at board meetings
- ○ Initiatives for management to actively engage in risk-taking (R&D, capital investment ,investment in M&A,business restructuring, etc.) and aggressive governance (building a system that encourages risk-taking)
- ○ Increase in the number of independent outside directors
- ○ Initiatives related to nomination and compensation of management including the CEO (establishment of nomination committee and remuneration committee, items to be discussed at remuneration committee and compensation committee and deliberation process, succession planning, introduction of performance-linked compensation and equity compensation, etc.)
- ○ Ensure board composition (use of skills matrix, etc.) and diversity to enhance board effectiveness
- ○ Efforts to stimulate deliberations at board meetings (review of items to be deliberated by outside directors, holding briefing sessions in advance, securing time for deliberations, appointing an independent outside director as chairman of the board, etc.)

[Engagement with the market (investors) (daily dialogue, exercise of voting rights, etc.)]

Does investor engagement have an impact on management behavior, managerial awareness, and corporate value?

- ○ What does the management side want from investor engagement activities? What is being done at the management, board, and working levels for each of these investor engagement activities for this purpose?
- ○ Are the statements in the governance report sometimes a topic of dialogue with investors? If so, which items?
- ○ Is there any dialogue with investors about the company's proposal, which was voted against by a significant number of investors?
- ○ How is the board involved in investor engagement activities (feedback of investor views to the board, dialogue between outside directors and investors, etc.)?
- ○ Do investors feel that they are exercising their voting rights and making investment decisions, including the details when explaining?
- ○ Do you think investors properly evaluate and sometimes encourage risk-taking by the company?
- ○ Are there any dialogues with investors that you feel have led to an increase in corporate value?
- ○ What is your overall assessment of investor engagement activities and challenges?

[Sustainability issues, etc.]

How do you address or intend to address the following issues?

- ○ Ensuring diversity in the company's core human resources (What is your assessment and issues regarding the company's approach to ensuring diversity in the appointment of core human resources, including the appointment of women, foreigners, and mid-career hires to management positions, and the setting of voluntary and measurable targets, and the publication of human resource development policies and internal environment development policies and their implementation status to ensure diversity?)
- ○ What is your assessment and issues regarding the quality and quantity of climate change disclosure based on the TCFD or equivalent international framework, the development of a basic policy on sustainability, and the disclosure of your company's initiatives?
- ○ What is your assessment and issues regarding disclosure of information on investments in human capital and intellectual property and effective oversight of the allocation of management resources, including investments in human capital and intellectual property?
- ○ What is your overall assessment and issues regarding the approach to stakeholders and sustainability in the Corporate Governance Code?

(End)

Interviews with companies: General comments on corporate governance (1)

Corporate Governance General remarks

[Significance of governance]

- **Governance reforms can make a significant contribution to corporate value in the long run.** Some say that governance reform does not lead to increased corporate value, but by separating management and execution and continuing governance reform, executives can focus on business execution with peace of mind, resulting in the creation of value. **From the perspective of dealing with scandals and family feuds, as seen in some Japanese companies, there are limits to executive-centered governance.** **It is important for the board to fulfill its supervisory function to create an environment where executives does not need to focus on extraneous issues and can concentrate on value creation.** [Chairman of the board]
- Although traditional Japanese companies are contrasted as stakeholder-centric with the shareholder-centric US model, in fact, many Japanese companies have failed to separate supervision and execution, and executives and the board are considered as an integral part of the company, and the state of the board is not a stakeholder-centric or shareholder-centric conflict, but an executive-centric or stakeholder-centric conflict. **The reality of governance in Japanese companies is an executive-centered approach**, in which the company passes the leadership role to the next president, so to speak, in what can be called ekiden management (relay management). Top management, who are linked with their predecessors, cannot deny precedents and cannot lead to increased corporate value. There will also be a mix of short-term and long-term issues. Becoming directors is an ultimate goal for most business people. [Chairman of the board]
- We want to be happy for all our stakeholders, and we believe that governance supports this. [Executive officer]
- **A solid division of roles between supervision and execution, and appropriate relationships (moderate tension, but cooperative) are very important**. The governance system is to create a system in which the executives do not have to think about anything else and focuses on execution and moves forward with speed. [Chairman of the board]
- It is the role of the executives to build a revenue base as the offense, while the basis of governance is defense. **The value of governance is to ensure transparent and appropriate processes so that the company can be trusted by those outside the company. Governance contributes to corporate value by preventing executive runaway and also by disclosing how it works.** [Board secretariat]
- Outside officers monitor management and provide opinions from various perspectives and insights in the formulation of management strategies, contributing significantly to the enhancement of corporate value. [Vice president]

[The ideal state of governance]

- In governance, it is **very important that the chairman of the board is an outside director**, and the question is whether this is functioning properly. **The chairman cannot understand the problem by looking only at the minutes of the management meeting; a time commitment is needed.** A “popular” outside director with many concurrent positions cannot fulfill the role. [Chairman of the board]
- **The basic approach to corporate governance is to ensure the mobility, appropriateness, and transparency of management, to fulfill its fiduciary responsibility and accountability to shareholders, and to work appropriately with all stakeholders**. [Chairperson and chairman of the board]

(Note) Positions are as of the time of the interview

Interviews with companies: General comments on corporate governance (2)

Corporate Governance General remarks

[The ideal state of governance (continued)]

- **The Corporate Governance Code is soft law**, and I always tell board members to **think about what policies are best for the company**. **For the "comply or explain" code, it is important for management to explain what they cannot comply with with their philosophy and principles.** [Chairman of the board]
- While we are aware of the Corporate Governance Code in our management, what we always have in mind is the realization of our philosophy and the happiness of our employees. We believe that **corporate value is generated by the material and emotional well-being of all employees**. It is important **to consider compliance and governance to achieve this.**[President and chairman of the board]
- **Not all US-style governance, such as having the board composed solely of the CEO and outside directors, is necessarily superior.** [Executive officer]
- Regarding group governance, **while our basic policy is to respect the uniqueness of the group companies, we also look at what we need to look at as a parent company.** For example, IT and cyber security are well managed by us for all group companies. We also emphasize important issues such as antitrust law and anti-bribery across the group. [Executive officer]
- When you have a variety of businesses like our company, each department has different risk areas and risk management approaches, so standardizing internal controls inevitably leads to conformity with the dominant department, which can be too much pressure for other departments. In order to solve these problems, we have established a **detailed governance system, which we call a field-oriented governance system, tailored to the actual conditions of each business unit and operating subsidiary**. [Chairperson and chairman of the board]
- **The governance structure must not fall into affirmation of the status quo, but must always look objectively at whether the current structure is good enough and seek to make it better**. For example, last year, we discussed whether we should remain a company with *kansayaku* board and concluded that we should. However, this year we would like to discuss what would happen if we were to transition to a company with a nomination committee, etc. In doing so, we believe that further assurance can be obtained as to whether the current structure is optimal under the current environment and business model. [Chairperson and chairman of the board]

[Assessment of the government's corporate governance reforms]

- **The government's corporate governance reforms have contributed to raising the level of governance in Japanese companies.** [Executive officer]
- We **appreciate the comply or explain format**, which allows for explanations such as "We have not yet done so, but we will work on it" or "We have a different view from the Corporate Governance Code." [Director]
- **The very good thing about the Corporate Governance Code is that, unlike the Companies Act, which is a mandatory law, the Code presents the concept, but allows each company to decide what to do.** Although we had complied with all items from the time the Code was formulated, there were some items that were just barely compliant, and the code was very helpful in considering what to do from that point forward. In addition, as the Code became more widespread, disclosure of approaches by other companies increased, and we were able to consider the most appropriate approach for our company while referring to them as well. [Board office]

(Note) Positions are as of the time of the interview

Interviews with companies: General comments on corporate governance (3)

Corporate Governance General remarks

[Assessment of the government's governance reforms (continued)]

- Before the Corporate Governance Code was established, the word governance had a strong impression of being defensive, but I am grateful that the Corporate Governance Code has changed my perception of governance as a means for growth. [Board secretariat]
- The Corporate Governance Code was the catalyst for thinking about it, and it is being passed on as organizational management. **We will change to a bullet train-type of management, where everyone is a driving force, rather than a locomotive-type, where only the founder is pulling the train.** [President and chairman of the board]
- The purpose of the Corporate Governance Code, which we see as strengthening the global competitiveness of Japanese companies as a whole, has had great strength in terms of improving profitability and the internal discipline on which it is based. However, we believe that **the code is a necessary condition for increased competitiveness, not a sufficient condition.** [Executive officer]

[Opinions on future issues of corporate governance reform]

- There is a movement called Board 3.0, but each company should create its board of directors in a way that maximizes corporate value. It depends on how well the companies hold themselves accountable. **Most of the matters related to corporate governance that should be accountable to stakeholders have already been incorporated into the Corporate Governance Code, so we do not believe there is a need to revise the Corporate Governance Code to make it more detailed than it is.**

  [Chairperson and chairman of the board]
- It is important to implement measures that one considers best in response to the currents of the world, and I **feel challenged to being judged good or bad solely on the basis of numbers from the outside**. I doubt that the level of governance will really be higher just based on the numbers. It is easy to superficially fulfill the requirements of the Corporate Governance Code, and creating of the skills matrix with skills that all the directors possess can be accomplished by just the person in charge. While some companies are taking the time to discuss these issues, including with outside directors, starting with what skills are necessary for their company, others may be taking a superficial and formal approach. **I am concerned that it will fall into just formal measures.** [Executive officer]
- Despite the delegation of various authorities to the executives, **if the number of items to be addressed in the Corporate Governance Code increases, the number of items to be brought before the board for corporate governance compliance will increase,** and there are areas where this is regressive. [Executive officer]
- As a company that has been autonomously working on governance reforms, we felt that the 2021's Corporate Governance Code re-revision seemed to weigh in on the execution side, requiring disclosures in line with the TCFD. **We believe that the Corporate Governance Code** should be restrained where execution is concerned. [Board secretariat]
- With regard to ensuring diversity in core personnel, **how to determine the ratio of women and mid-career hires is not so much a governance issue as it is an area of management judgment by the executives.** [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: General comments on corporate governance (4)

Corporate Governance General remarks

[Opinions on future issues of corporate governance reform (continued)]

- Regarding the diversity of core human resources, women, foreigners, and mid-career hires are mentioned as examples, and this seems to be the perspective of domestic efforts. **There is the question of how to think about foreigners and mid-career hires when considering this subject on a global basis.** [Board secretariat]
- Regarding the diversity of core personnel, although women, foreigners, and mid-career hires are mentioned, **as each company has different characteristics and business activities, the personnel required in terms of work experience,age, and skill sets are also different**. [Board secretariat]
- **While board diversity is important, the first step is to appoint the right people to serve on the board**, and attributes such as gender and nationality should not take precedence over this. [Board office]
- I was surprised to see that the revised Corporate Governance Code for 2021 includes new items such as IP, TCFD, and mid-career hires. I understand the purpose of the addition, but the number of relevant departments within the company has increased and the burden of disclosure is high. **It is important to hold substantive discussions with relevant divisions to ensure that disclosure does not become the objective and become a mere formality.** [Legal department and board secretariat]
- Although it is assumed that the comply-or-explain apply, in the end, the world trend forces us to move to the comply side. However, there are companies that are formally compliant with the Corporate Governance Code but have been involved in scandals due to ineffective governance. Because prioritizing the formal aspects could lead to a reversal of the main intent, we should put forward a concept that emphasizes the substantive aspect. [Board secretariat]
- **There were principle(s) for which it was unclear whether we were compliant or not, so we explained this honestly and showed the way forward.** I had heard at seminars for companies that even if companies fully complied, investors are not looking at that and that a thorough explanation should be given, so we were able to explain without having concerns. [Executive officer]
- Although the rule is comply or explain, **there are times when I feel pressure to make everything compliant.** In particular, requirements regarding a director‘s age, professional experience, and gender may not always be compatible with the qualities a company seeks in a director at a given point in time. [Corporate planning department]
- There is no point in reducing profitability and strengthening only the defense. In order to improve the level of governance, it is necessary to have a reasonable staff, which will cost money, and the company must be large enough to absorb that cost. Therefore, the listing criteria for the prime market, which requires a higher level of governance, should be further raised.

  [Chairperson and chairman of the board]
- It is good to utilize outside directors, but increasing the number of outside directors all at once will create problems of shortage of human resources and dual appointments. **We need to find our position based on the maturity of the company and the level of human resource development.** [Executive officer]
- More and more investors are establishing bylaws regarding the tenure of outside directors. Furthermore, there are concerns that if **more than half of the directors should be outside directors, it is possible that unqualified people will become outside directors**, which would run counter to governance reform. [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: General comments on corporate governance (5)

Corporate Governance General remarks	[Opinions on future issues of corporate governance reform (continued)]

Corporate Governance General remarks

[Opinions on future issues of corporate governance reform (continued)]

- While we understand the importance of capital efficiency and other indicators, they vary by business type, and **long-term efforts to improve social value do not immediately lead to profits.** We believe it is important to evaluate corporate value in terms of both social value and economic value. [Vice president]
- **With regard to sustainability, it is difficult to draw a line between governance and execution**. I don't disagree that the board should discuss the management principle-level talks, but what about individual specific policies that should be further considered based on the management principles? For example, if the sustainability policy is to include a working level discussion about measures against climate change and the point of influence on the supply chain, this should be considered more by executives. Regarding sustainability, there is a trend toward increasing the content of disclosures, and we believe that drawing a boundary with execution side must be carefully monitored. [Executive officer]
- **Although the Corporate Governance Code states that cross-shareholdings are supposed to be reduced, the actual situation is more individualized and specific**, and for example, for shareholdings that are not cross-held but have a special history, a certain level of understanding has been obtained in dialogues with investors. On the other hand, some voting advisory firms make mechanical judgments regardless of the content of disclosures, which may require classification and redefinition of cross-shareholdings. [Vice president]
- The appropriate governance structure varies depending on each company's business type, nature of business, and staffing structure. In order to utilize the positive aspects of individual companies to strengthen competitiveness, we would like the guidelines to be established by carefully considering the balance between the areas where individual company ideas should be respected and the areas where reforms are required of all companies. [Board secretariat]
- As the board secretariat, we are having a very difficult time explaining to top management what is required by the Corporate Governance Code as we proceed with our response to the Code. For example, it is difficult to understand what terms such as human resource strategy, intellectual property, and human capital refer to, and in some situations it is difficult to know how to interpret them. **If the Financial Services Agency prepares an executive summary that summarizes the key points and interpretations of the Code in an easy-to-understand manner, it would make it easier to explain the Code to top management and encourage them to take a more proactive approach to governance reform.** [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (1)

Enhancing board independence

- As the market shifts from domestic to overseas markets, we have introduced outside directors because we believe it is necessary to engage in business with the broad knowledge of third parties. **The introduction of the system has not only allowed the company to obtain business advice from an outside perspective, but has also enabled monitoring to function, so that things are no longer decided solely on the basis of a single word from the president**.
- **In addition to our directors giving presentations on our business to the outside directors, we also provided them with opportunities to visit the factories of our major customers to deepen their understanding of our business by helping them to understand how our products are used**. As a result, more appropriate advice was given, and for example, when making decisions on individual deals, such as M&A above a certain size, we were able to receive opinions not only on whether the M&A is appropriate and whether the price is fair, but also advice such as "this type of collaboration might be possible if this company were to be acquired."
- In addition, while the agenda and minutes of management meetings have been distributed to outside directors for some time, a year ago we changed the system to one that **allows them to observe management meetings in person**. In addition, **the camp**, where executive officers discuss immediate issues and future business strategies, **is now open to outside directors, and the camp is recorded and made available for viewing for approximately two weeks.** This has improved the substance of the discussions, as it has allowed the board to save time for explanations and have more time for discussion.
- When a wide-ranging discussion is desired but cannot be discussed at a board meeting because minutes are kept, **a free discussion period is held after the board meeting.** The executives include even department heads, and the discussions are more in-depth than those of the board, transcending positions.
- The board secretariat works with the chairman to figure out how to efficiently meet everyone's needs in board meetings that have a limited number of meetings and time. For example, typical measures include **distributing the agenda in advance and explaining the agenda in advance,** thereby shortening the amount of time spent explaining the agenda on the day of the meeting, **and accepting questions in advance** and answering them ahead of time.
- Since 2 or 3 years ago, we have been holding regular **1-on-1 meetings between the so-called lead outside director, the president, and the chairperson for about an hour each time.** During these one-on-one meetings, we openly discuss the direction of the company and the board of directors, and the content of these discussions is reflected in the operation of the board of directors by internal directors, outside directors, and outside *kansayaku*, respectively. There are some things that cannot be said in front of everyone, so during 1-on-1 meetings, we can express our thoughts to each other, get advice, and deepen mutual understanding.

[Board office]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (2)

Enhancing board independence

- **In order to deepen the discussion at the board, it is necessary to have in-depth discussions by executives to identify issues**. Because the size of the company's management meetings had increased and business reports had become the main focus, **the number of members of the management meetings was narrowed down** so that in-depth discussions could be held in the management meetings.
- With regard to the board, the increasing importance of outside directors has necessitated formal and informal information and training to encourage good discussions by outside directors. Therefore, **we have set up a dedicated support department** and have begun to provide orientation to directors. In addition, since a wide variety of matters are brought before the board, the secretariat organizes the information and then presents it to the board.
- In terms of encouraging risk-taking by executives, **outside directors with a management perspective advise the board on both risk and growth**, and they encourage us to promptly take opportunities for capital investment and such. For example, in discussing the sale of one business, the board debated why the company would sell a business that is currently performing well. At that time, the outside directors severely challenged our internal logic from the perspective of whether we could fulfill our accountability to investors as a growth strategy, and we discussed this issue with the board about eight times until we obtained their approval. During the discussions, the executive side also reexamined the situation and made improvements, such as improving the sale price and leading to business alliances and collaborations with the buyer.

[Board office]

- **The board, entrusted by stakeholders, has the responsibility to establish a system that allows the executives to focus on business execution.** Rather than appointing people who are convenient for the executives as outside directors, the organization must meet the expectations of investors, who want to see the creation of an environment in which execution can easily focus on business execution. To this end, it is necessary for the board to fulfill its functions, and the following initiatives are being implemented at the company: the management committee, the outside directors' meeting, and the board discuss the issues raised, and by the next meeting, the executive committee reviews the issues raised. These discussions allowed us to understand the details of the case and added depth to the discussion.
- Since a large information gap between the board and the executives prevents good discussions, we have been holding **non-binding outside directors meetings** for more than 10 years **to correct the information gap**. The meeting is held two business days prior to the board meeting, at which the executives explain the agenda and outside directors freely ask questions to identify issues and gain an understanding of the nature and background of the agenda items.
- **The chairman of the board requires a time commitment**, and the chairman himself is present at all committee meetings and management meetings related to risk management and sustainability. The chairperson‘s attendance at these meetings allows him or her to make responsible decisions in selecting and setting the board’s agenda. It enables him/her to understand the matters that should be discussed by the board among the executive decision matters, and to design the discussions of the board. For example, items that need to be commented on from a variety of viewpoints at the board meeting are made into report items, items that need to be decided after several discussions are made into items for deliberation, and items that need to be decided at an early stage are put on the agenda for the board meeting as resolutions.

[Chairman of the board]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (3)

Enhancing board independence

- One of the innovations I have made as chairman of the board is **to emphasize unanimity in proceeding with the meeting, because even if it were legally possible, going ahead based on a majority vote is often problematic.** In addition, while board meetings often tend to be a composition of outside directors versus internal directors, the company's secretariat makes every effort to ensure that outside directors can discuss issues on the same level as internal directors by, for example, briefing outside directors in advance and holding opinion-exchange meetings exclusively for outside directors. Thanks in part to these efforts, outside directors are now able to discuss issues at the same level as internal directors, and there have been cases where a proposal that was put before the board was ultimately withdrawn due to opposition from outside directors.
- **Some Western investors find it difficult to understand how a board is functioning in a company with a *kansayaku* board. However, if we explain that operating a board of directors with an emphasis on unanimity is practically the same as giving outside directors veto power, and that it is actually more effective than having a majority of outside directors only formally, with specific examples as described above, they are often properly convinced**.

[Chairperson and chairman of the board]

- Since outside directors are in the majority on the board and the chairman is also an outside director, the environment is one in which outside directors can speak freely, and we have received a variety of suggestions. **The board's remarks are managed separately from the minutes of the board meetings by preparing a management chart of remarks**, and the chairperson and the executives confirm the contents of the chart. To ensure that opinions and suggestions made at board meetings are not left unaddressed, items requiring action are thoroughly summarized, checked by the chairman, chairperson, and president, and followed up by assigning them to items to be reported or discussed at the next board meeting. For example, the board has pointed out the need to strengthen the functions of the corporate division from a market-in and global perspective, as well as the need for company-wide marketing efforts, which has led to actual initiatives.
- The role of outside directors on the board has become extremely important, and **since it would be problematic if all outside directors were replaced at once, the composition of the board has been designed with diversity in terms of tenure in mind, so that the replacement of outside directors will occur gradually.**

[Board secretariat]

- **For the purpose of correcting the information gap between independent outside directors and internal directors and communicating information from the executives as early as possible, a meeting of independent directors has been established and is held almost every month**. As a forum for the free exchange of opinions, rather than a decision-making forum, management policies and other matters are first presented in draft form to the independent directors' meeting to receive opinions, after which they are resolved by the board. In addition, the company has gone further from the independent directors' meetings where the executive side presents drafts, etc., to hold **private sessions after monthly board meetings where discussions are held solely by independent directors, as well as 1-on-1 meetings between the chairman and president, and the president and independent outside directors**.

[Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (4)

Enhancing board independence

- The number of directors was reduced to half so that they could be more flexible. In addition, the number of outside directors was increased in order to listen to outside opinions as well as internal logic. Now the chairman of the board is also an outside director. Outside directors commented that this has made it easier for them to speak up. **I thought it was not a matter of the number of people, but the ratio does matter.** In addition, by internal directors requesting opinions from outside directors, outside directors are able to speak up without hesitation. As a result of these efforts, outside directors now speak more frequently during questioning sessions, and outside directors are able to take the initiative in discussions.
- **Newly appointed outside directors are given lectures about systems and governance prior to their appointment**. In addition, the chairman of the board attended the management committee meetings and shared the discussions at the management committee meetings with the board, thereby deepening the understanding of outside directors. In addition, we provide opportunities to visit business sites and invite outside directors to meetings on research and development, on which we are focusing our efforts, to deepen their understanding of our technology and enhance the deliberations of the board.
- **Voluntary meetings of only outside directors, with no secretariat involvement at all, and informal meetings between the president and outside directors are also held**.

[Legal department and board secretariat]

- Thanks in part to the work of the outside director serving as the chairman of the board, there is active communication among outside directors, including outside *kansayaku*. One of the comments from an outside officer was that "internal officers often seem to be willing to learn from outside officers." **By outside officers having a sense of unity, and internal board members trying to learn something from them, it creates a sense of unity among the board as a whole, leading to improved governance, management, or monitoring.**

[Executive officer]

- In the past, board meetings often simply confirmed matters such as capital investments decided by the management committee, but now the main agenda items are related to the company's plans and policies, such as the environmental vision. I believe that outside directors did not even have to speak at the board meetings with the previous quick and efficient ways of handling things. However, **in today's board meetings, outside directors are increasingly asking questions about the content of the agenda, which has led to more advance briefings to outside directors as needed.** We also receive inspiring comments from outside directors such as, "given the state of the industry, the funds from the sale of cross-shareholdings should be used to invest in the creation of new associates."
- **Since questions about prerequisite knowledge at board meetings can result in extra time and less time for deliberation, the board secretariat tries to prepare materials that are easy for outside directors to understand, such as by increasing the number of explanatory notes on basic terms in materials on the subjects of the board meetings**. Nowadays, if the documents are difficult to understand for third parties or outside directors, they may not even pass the management meeting.

[Board secretariat]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (5)

Enhancing board independence

- From the perspective of separating the presentation and deliberation, announcements of business results and the status of group companies are made at the management meeting, which is attended by outside directors, prior to the board meeting. In the evaluation of the effectiveness of board meetings, there was a request that materials be distributed in advance in order to facilitate active discussion at the meetings, and the company has begun **holding advance briefings and distributing materials in advance for important matters**. Through these efforts, information is properly shared with outside directors, enabling them to make appropriate decisions.
- At board meetings, the **chairperson particularly asks outside directors for their input, which stimulates discussion**. In addition, the audit committee has less members than the board, which allows for more candid opinions to be expressed. At these meetings, outside directors began to offer a variety of points of view, including opinions from the perspective of shareholders and management, as well as from the perspective of environmental impact. These comments and suggestions made us realize that companies are viewed in many different ways, and we feel that we need to properly explain our efforts. [Director]

- To enhance the deliberations of the board, the company trains outside directors and also distributes pre-review materials several days prior to the board meetings and provides explanations in advance. After the appointment of outside directors, they spend a year deepening their understanding of the corporate philosophy and each of the company's businesses. Specifically, the program includes a two-day and one-night camp program that includes classroom lectures and factory visits, as well as a visit to the foundation memorial museum. Because the board deepened their understanding of the corporate philosophy through this training, they were able to make the decision to sell a business that was not unprofitable on the company's business portfolio, based on the corporate philosophy and the concept of best owner, considering the future happiness of the company and the employees in the business, and the desirable form in terms of contribution to society.
- The deliberations of the board were enhanced, and useful opinions were obtained from outside directors. For example, when discussing the business portfolio and what businesses to focus on in the next two to three decades to achieve sustainable growth, the outside directors expressed the opinion that it is difficult to create new businesses from scratch, that acquisitions through M&A are more efficient, and that the company should engage in M&As more frequently.
- In addition, **as the deliberations of the board are enhanced, the level of content and documentation of matters presented by the president to the board will also be required to be improved. This raises the level of the executive, and the board of directors and the executives engage in friendly competition with each other.**

[Board secretariat]

- If we suddenly raise a matter to the board, the discussion will become abstract, so we ask outside directors to join the management committee as observers. [Executive officer]

- In order to familiarize outside directors with individual issues and give them prior knowledge, the company has been making efforts to provide explanations in advance of board meetings, meetings of outside directors and opportunities to actually see the site, which has led to enhanced deliberations at board meetings. [General affairs department]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects on enhancing board independence (6)

Enhancing board independence

- Based on feedback from the effectiveness evaluation, the following improvements have been made to enhance the understanding of outside directors.
  - **Distribute materials early, conduct briefings for outside directors the day before board meetings, and hold outside directors meetings**
  - **Explanation of business plans, medium-term management plans, etc. to outside directors and outside corporate auditors prior to the submission of proposals to the board.**
  - For several years now, **all directors and all *kansayaku* hold free discussions in the form of debates that do not aim to reach a conclusion.**
  - To facilitate understanding of our complex business, we **present the strategic position of each business unit before explaining individual projects.**
- As a result of these efforts, the understanding of the company by outside directors has deepened, and opportunities to receive opinions based on a variety of knowledge have increased. In addition, some matters have been discussed many times by the board due to input from outside directors. The opinions of the external officers certainly contribute to the quality of the projects.
- In response to comments from outside directors at board meetings, an agenda was re-addressed about three times, and in other cases, an agenda was withdrawn. **While the deliberations were productive, they also required attention to time management.**
- **We believe that it is good for outside directors to hold office for a certain length of time, as they take time to deepen their understanding of the company**.

[Board secretariat]

- At the time the Corporate Governance Code was formulated, materials for the board meetings were distributed the day before the board meetings, but **now they are distributed electronically three business days prior to the meetings to enhance the deliberations of the board**. Other documents for decision-making and management meetings are also made available in electronic media**. Other opportunities are provided for outside directors to meet with directors, senior executives, and younger employees** so that outside directors can understand the actual situation within the company.
- Regarding the critical decision of business withdrawal: from the viewpoint of only those within the company, the decision to continue the business seemed reasonable at first glance, and prior to the governance reforms, there would have been a strong voice in favor of continuing the business. However, the number of outside directors, which has increased as a result of governance reform, raised questions about the rationale for continuing the business, and the executives were also affected by the impact of contact with outside directors, as they understood what kind of knowledge and thinking outside directors use to make decisions. These resulted in the decision to withdraw from the business.

[Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the division of roles with the executives (1)

Division of roles with the executives

- **The key to management is speed. In order to improve management speed, a cycle of empowerment and transparency should be established in which the board holds the main authority, that authority is transferred to the executive committee and then to each business unit, and once the authority is transferred, it is implemented properly and reported to the board.** The company's empowerment and transparency cycle, described below, has allowed the board to spend more time considering important issues related to the management of the company, rather than deliberating on individual matters.
- **In order to transfer authority to the executives, the executive side must be trusted by the board.** When the executives take the board's input seriously and take action, a sense of mutual trust is fostered, and the cycle of empowerment and transparency begins to turn. For example, in the reform of our company's management committee, the line heads of each business were removed from the membership of the management committee, which now consists of the leaders of corporate divisions and representatives from the acquired company, and the number of members was reduced to ten. By adopting such a structure, the proposer will be asked at management meetings, for example, "Have you considered environmental issues?", "Have you looked into the cost aspect?", or "Have you considered the investor's point of view?", and the proposal may be rejected by the management meeting. The contents of the business plan and the medium-term management plan are also thoroughly discussed at the management meeting and proposed to the board. **This substantial discussion at the management meeting allows the board to feel that the executives are thinking clearly,leading to trust in the executives and a transfer of authority**. When management meetings are held in the presence of the president, group thinking stops. Animated discussions at management meetings can help the executive side gain the trust of the board and lead to a transfer of authority.
- Similarly, each business unit gains the confidence of the management committee, which transfers authority to the business units. This enabled the business units in direct contact with customers to make decisions quickly, which in turn led to improved performance.
- In addition, the business units that received the transfer of authority were **accountable to the management committee, the management committee to the board, and so on, and this had the effect of creating a sense of mutual responsibility and identity as members of a team**.

[Chairperson]

- **The authority for important business execution decisions, such as transaction matters, was delegated from the board to the executives, to the extent legally possible**. For example, with regard to investment, the board decides which areas to invest in and the budget for each department, but the executives are free to decide on the rest as long as it is within these limits. However, there were some concerns as to whether transactions worth several hundred billion yen could simply be reported to the board, so as an exception, the board can decide on matters that the chairman of the board has decided should be discussed by the board or that have been proposed as such by individual directors.
- The most recent medium-term management plan has been formulated after more than one year of deliberation by the board, and after it has been formulated, the board confirms its progress and examines issues such as whether investments are sufficient.

[Corporate planning department]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the division of roles with the executives (2)

Division of roles with the executives	

Division of roles with the executives

- **Since monitoring by the board is meaningless if not done frequently**, the status of business execution is reported at monthly meetings of the board. The contents of the reports were initially only formal reports of income statement items, but now we have a **system in place to report more business-oriented specifics,** such as what kind of events are occurring in which areas, for example, how the semiconductor shortage is affecting our company, what kind of areas are being affected by the coronavirus, and what measures are being taken to deal with the situation. As a result of the concrete, business-oriented reporting, directors and *kansayaku* are now examining risks and other issues based on concrete information, and are voluntarily gathering information, such as listening to financial results briefings and reading reports from institutional investors, and using this information in their discussions.
- **Discussions that contribute to medium to long-term improvement of corporate value are difficult to prepare in advance, so when setting the annual agenda, it is decided in advance in which months medium to long-term discussions will be held.** Toward this end, the business execution side is taking the lead in preparing materials for discussion, and the day of the meeting is shaping up to be a very in-depth discussion. At first, we had the board involved in the formulation of the medium-term management plan, but since our business cycle is longer than that of other companies and we cannot dynamically change the structure of the company within the period of the medium-term management plan, we now ask for their opinions on the business direction five or ten years into the future. [Board office]

- **In preparing the medium-term management plan, based on the opinions of the board in its effectiveness evaluation, the board first projected the future shape of society, discussed the long-term direction of the company, formulated a long-term strategy, and then backcasted the plan from said long-term strategy**.
- **Regarding how the monitoring function of the board should be exercised, both outside directors and *kansayaku* commented that monitoring through discussions of specific projects would be more accurate than discussions of medium to long-term strategies alone. The board's focus on medium to long-term strategy means that it discusses how the overall vision and plan are designed and where individual projects fit into the plan. Based on this approach, the board confirms the progress of the medium-term management plan each year and the executives are monitored, receiving advice and verification from outside directors.** [Board office]

- In the past, many of the directors were internal directors who were also in charge of business execution, so board meetings were mostly harmonizing, and many resolutions were merely formalities. Therefore, in addition to items to be **resolved and reported, items to be discussed by the board, such as medium to long-term issues, items that are likely to become issues in the future, and progress in the medium- to long-term management plan, are determined in advance as annual plans**, so that the board can devote time to discuss medium to long-term issues.
- **The annual plan for the board should be planned to cover all important matters and not only those that the executive side wants to discuss,** so that the board can thoroughly discuss what it thinks is necessary from a long-term shareholder perspective. To make such a plan, it is essential that the chairman of the board be an outside director. As a result of these efforts, the board has been able to engage in robust discussions from a medium to long-term perspective, and the executives' discussions and decisions based on these have led to reforms that have increased corporate value. [Board secretariat]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the division of roles with the executives (3)

Division of roles with the executives

- The chairperson (outside director) provides input on the draft of the annual agenda for the board prepared by the president and the secretariat and finalizes it. When preparing the draft, a regular agenda is set at the beginning, and then time is set aside for medium and long-term agenda items such as management plans. **The board has repeatedly discussed major medium and long-term issues such as the medium-term management plan and ESG strategies, not only discussing their formulation but also how to move them forward, such as requesting the executives to check its progress**. [Legal department and board secretariat]

- While taking into consideration the opinions of outside directors as to whether this is something that should be discussed by the board, we have gradually increased the delegation of authority to make business execution decisions as the company has expanded, in order to prevent the board from being too busy with business execution matters to be able to discuss medium to long-term issues.
- **The effect of delegating decision-making authority for business execution has been very significant in terms of increasing the effectiveness of the board**. As delegation has progressed, the board has been able to focus its discussions on medium- and long-term issues. At the same time, **the promotion of delegation will also strengthen monitoring, since we cannot deny what we have decided to delegate ourselves after the fact**.
- **Discussions on medium and long-term issues are systematically divided into company-wide and theme-specific discussions (for example, IT or ESG).** It is the job of the secretariat to come up with the initial topics for discussion, and they set up an annual schedule and suggest how we can discuss them. [Executive officer]

- Regarding the division of roles between the board and the executives, the **president has announced, "Let's change the mindset of us, the executive side so that the executives, not the board of directors, are responsible for making decisions regarding business, and the board supervises and advises** them. As a specific initiative, the company reviewed proposals to be submitted to the board and delegated authority to the executive side for all items other than those to be approved by statutory resolution. For example, personnel matters and small investment projects of group companies used to be resolved not only by the executive committee but also by the board, but internal rules were changed to give the executives the authority to make decisions. Investment projects that exceed a certain amount are reported to the board, but other projects are rarely resolved at the board meeting. Fewer items on the board's agenda require only procedural approval, and as a result, there is more discussion of what is on the agenda, and the board's discussions are more substantial and more useful advice is available. Specifically, they now spend more time discussing issues such as compliance and whether the company has the necessary resources and systems in place for quality-related matters, and they are increasingly aware of the perspectives of these outside directors during the executive review stage. In addition, the board is now able to devote more time to reviewing major policies and checking the progress of the medium-term management plan, and the board often discusses governance-related agenda items that were rarely discussed at board meetings prior to the formulation of the Corporate Governance Code.
- The progress of mid-term management plan is discussed at the board by business area, however, since **the time of regular board meetings is not sufficient to discuss long-term management issues, in addition to regular board meetings, the company uses one weekend day to provide an opportunity for all directors to discuss medium- to long-term strategic themes.** [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the division of roles with the executives (4)

Division of roles with the executives	
	■ In the past, the board was mainly operated by the executive side, but we are coming to separate execution and supervision, as an outside director commented that the role of the board should be a forum for discussion of strategy and governance. We believe that by making the board a place to receive monitoring by stakeholder representatives and concentrating business execution authority largely in the hands of the executive team, management can be carried out smoothly and quickly. For example, **the medium to long-term growth strategy meeting (twice a year) is held separately from the board meetings, and is attended by executive officers and directors, including those from outside the company, to discuss issues such as the ideal vision, what the company should be, its business model, what contribution it should make to society, and human resource development.** Through these meetings, the knowledge and experience of the outside directors were reflected, and the outside directors were able to get more inside the company and evaluate the company from an external perspective. Together with the transfer of authority to the executive side, this is enhancing management capabilities. ■ **Could there also be measures to motivate employees to move up the ladder by, for example, having executive officers who are paid higher salaries than directors so that their aspirations for executive positions are motivated?** [Executive officer]
	■ We consider **our governance structure to be based on the establishment of an appropriate executive structure**. The general managers of the business divisions are placed directly under the CEO, who is the chief executive officer, and the officers in charge of each business are placed between the CEO and the general managers of the business divisions as an intermediate level and are not responsible for execution. This is because there is a risk that if the controlling officer is made the executive officer, individual optimization may occur and that some things may be omitted across different business areas. We believe that this executive structure is appropriate for our company, which has many business divisions, because it allows for ad hoc collaboration among business divisions and the creation of internal JVs. While one measure is to reduce the size of the board in order to increase the ratio of outside directors, the company's executive structure as described above allows the controlling officers to have membership in the board in order to have them play a role in discussions from the perspective of the entire company, rather than as representatives of the interests of individual business units. [Chairperson and chairman of the board]
	■ With an emphasis on a structure in which the executives implement projects and the board supervises them, important progress on individual projects approved by the board has been reported to the board for a long time. Recently, the importance of such matters has been judged more strictly, and progress reports are made to the board on matters that may have a significant impact on the project, even if they were not previously reported, and as a result, the executives are now more aware of the board than before. [Board secretariat]
	■ The reality is that internal directors are more knowledgeable about decision-making for individual projects. **Discussions on the company's overall strategy, such as how to address ESG issues in the future, are more actively discussed by outside directors and are more conducive to management.** [General affairs department]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to management nominations (1)

Management nominations

- **Only executives can increase corporate value. What the board can do to this end is to create that environment. One of these is the nomination of the president.** This requires internal confidence in the nomination committee. Confidence in the nomination committee gives legitimacy to the organization for the selection of the president, and at the same time, the fact that the president was selected by the nomination committee allows the executives and the president to exercise their power without unnecessary reservation on behalf of their predecessors. **In order for the nomination committee to gain trust within the company, it is necessary to know the executives well.** Therefore, the nomination committee is not involved in the selection of the president only at the final stage of selecting a successor, but rather the nomination committee members spend time interviewing and with all of the candidates from the initial stages of succession planning. [Chairman of the board]

- Although the president is responsible for training potential successors, it is the nomination committee that selects the successors, and we ensure that **the president is not a member of the nomination committee**. By not allowing the president to decide on a successor, the new president can implement reforms on his or her own initiative.
- **The abilities required of a president vary from time to time.** Therefore, the nomination committee defines the requirements for selecting the president based on the understanding of outside directors of management issues through training when they are newly appointed, discussions at outside director meetings, deliberations at board meetings, and attendance at executive management meetings. [Board secretariat]

- When selecting the president, a voluntary nomination committee **first discussed what qualities were required of the next president**, and then narrowed the field of candidates. **Committee members are given the opportunity to have direct contact with the candidates, such as by inviting the candidate to attend meetings,** so that they can understand the candidate's qualifications and aptitude.
- In introducing the skills matrix, there were some doubts at first whether the actual situation would be well conveyed in the form of rounding, and the idea was not to use a matrix but to list skills in the reasons for appointment in the convocation notice, so that when read together with the text, it would be possible to see who possessed specific skills. However, as the number of companies disclosing a skills matrix increases, we decided to disclose them in a matrix because of the opportunity to get feedback from investors and the benefits of listing**. A major outcome of the skills matrix study was that we were able to discuss what skills are needed for our current board**.

[Legal department and board secretariat]

- Succession planning is discussed by the nomination advisory committee, not only for the president, but also for executive officer candidates. **For executive officer candidates, HR is working to increase the population by creating a long-term human resources development plan, and outside directors may have opportunities to discuss and screen candidates**.
- **For the current president, discussions are being held on reappointment based on the evaluation system**. Basically, to stay in office is never unconditional, and a decision for them to stay in office or not is based on a quantitative evaluation and a qualitative evaluation by outside directors. [Board office]

- **The fact that the person in charge of a project explains the project at a board meeting also serves as an opportunity for outside directors, who are members of the nominating committee, to assess the qualifications of a potential successor, such as whether the person in charge can tell a cohesive story about the project as a future manager.** [Board office]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to management nominations (2)

Management nominations

- The nomination and remuneration committee includes three outside directors, and **just having outside directors on the committee has resulted in the committee members questioning themselves whether the decisions are self-serving or not.** Having outside directors on board makes sense as an opportunity to consider reasonableness as a criterion.

  [Executive officer]

- The appointment of the president is the most important matter in governance. **Based on the viewpoint that only management can choose the management of the company, outside directors are appointed from among those who have served as presidents of the company.** Not only the nomination of a president, but also the sale of a business or M&A process requires the management's perspective. The nomination committee is also considering the qualities required of outside directors for the succession of outside directors. [Board secretariat]

- The nomination committee holds substantive discussions and oversees nominations and appointments, including the CEO succession plan. For example, **the committee discussed whether it was appropriate to replace the current CEO at this time, what kind of person should succeed him, and whether an outsider should be considered as a candidate.** The nomination committee members, who are outside officers, are invited to attend a camp, which the candidates also attend, to get to know them better and to see the personalities of the candidates. [Chairperson and chairman of the board]

- **The nomination committee is composed of internal directors who are familiar with the personnel within the company, as well as outside directors with business experience, to avoid shallow discussions, and *kansayaku*, who have strong authority to dismiss the CEO and other officers under the Companies Act. This ensures quality in terms of both legality and effectiveness**.
- It is also important to provide input to the nomination committee members with the necessary information for the nomination committee to perform a full deliberation. Specifically, in addition to the consideration given in the preparation of materials, many opportunities are set aside for the nomination committee members, who are outside officers, to get to know the candidates well and to see their personalities. Based on this input, the process of narrowing down the long list of candidates to a short list was conducted with input from each committee member on what perspectives and reasons made the person desirable and how he or she perceives the business environment. [Board secretariat]

- In Japanese companies with a nomination committee system, a committee consisting of some directors has the final decision-making authority regarding nomination and remuneration. However, **rather than having only three or four people involved in major decisions such as the election or dismissal of the president (or a succession plan), it would be more appropriate to have the board maximize the use of outside expertise.** [Company with *kansayaku* board]

- Initiated efforts to evaluate the effectiveness of the board in response to the Corporate Governance Code. Currently, the company is also going into the **evaluation of individual officers**, including evaluations of the chairperson and self-evaluations of the directors and *kansayaku* themselves. [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the evaluation of the effectiveness of the board (1)

Evaluation of the effectiveness of the board

- If the board believes that it has a responsibility to its stakeholders, it would naturally want to undergo an evaluation of the board's effectiveness to determine whether its efforts are appropriate. **The evaluation of board effectiveness is a must, without which governance reform will not proceed. Another key point is the existence of a PDCA cycle for improving the effectiveness of the board, and it is important to address how the results of the evaluation of board effectiveness have been used to reform the board with continuity.**
- **In our effectiveness evaluation, we use overseas standards as benchmarks, and also conduct assessments based on themes determined each year**. These effectiveness evaluation efforts serve as a driver of reform, and through the effectiveness evaluation, we discuss what needs to be done in governance reform and implement reforms. For example, with regard to the composition of the board, there was a comment in the effectiveness evaluation that simply creating a skills matrix was not sufficient. Therefore, the board has discussed this issue several times, and **as an effort to go one step further from the skills matrix, the company has established criteria for the qualities and skills required of chairpersons, outside directors, and others**. Such criteria can also serve as a reference for directors as to what is expected of them in their role, as well as a basis for individual evaluation of directors and guidelines for the reappointment or non-reappointment of directors.

[Chairman of the board]

- Board evaluations are conducted annually, with an external evaluation conducted once every three years. The opinions of directors and *kansayaku*, both internal and external, who attend board meetings are heard in the form of questionnaires. **At the beginning of the third-party evaluation, in addition to the multiple-choice questionnaire, the contractor conducted individual interviews with each director and asked them to report good points and areas for improvement**. Based on the report, the chairperson and secretariat took the lead in preparing a rough draft of what to do over the next year, which was discussed at the board meeting and worked on for one year. The next year, they conducted a self-evaluation and wrote down how it went after running it for a year, and **by keep running the PDCA cycle, the quality of the board meetings is gradually improving**.
- The good thing about multiple-choice is that you can see changes over time. For example, we continue to ask questions such as, "Has the quality of board discussions improved compared to the previous year?" For example, look at the 5-year trend, and if the score in the evaluation is declining, it means there is a problem, so we conduct a cause analysis.
- Although the volume of answers to open-ended questions becomes quite large, the responses obtained are distributed to the board members as the board evaluation report without summarizing or processing them in any way. The members are interested in what other members think, so even though there are many pages, all directors read them all carefully, and we are able to discuss what to do for the next year. Since people write things honestly, the members will have a better mutual understanding of each other and be able to discuss issues based on this understanding.

[Board office]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to the evaluation of the effectiveness of the board (2)

Evaluation of the effectiveness of the board	
	■ The chairman of the board is the executing entity for the effectiveness evaluation, and the corporate planning department prepares it as the secretariat. The analysis and evaluation of the responses are submitted to the board for deliberation and resolution. ■ **The voluntary nomination and remuneration committee is also evaluated for the question "Is the committee being used appropriately?" in the evaluation of the effectiveness of the board. A separate evaluation of the effectiveness of the audit committee is also conducted.** [Corporate planning department]
	■ **Based on the annual effectiveness evaluation, the company recognizes issues and determines priority themes, addresses the priority themes in the following year. This process is repeated.** One example of how priority themes established based on the effectiveness evaluation have led to increased corporate value is in the area of sustainability. In response to the identification of sustainability as a priority theme for the next period in the effectiveness evaluation, the board established a basic sustainability policy, sustainability goals, and organized materiality. Based on this, sustainability initiatives have been promoted and have led to increased corporate value, for example, the inclusion of the company in many ESG indices, which has led to an increase in the company's share price. [Board secretariat]
	■ Before the Corporate Governance Code was formulated, each director had been giving his or her impressions of the past year at board meetings, and since the introduction of the effectiveness evaluation under the Code, the effectiveness evaluation has been conducted by incorporating a questionnaire in addition to the director's impressions. ■ **The questions for the effectiveness evaluation questionnaire are designed by the Secretariat after consulting with the chairman of the board.** The format is basically free entry, and we have received candid feedback. **We considered incorporating a 5-point scale, but have not adopted it because we believe that each person has his or her own criteria**. The responses obtained are compiled by the secretariat into an analytical document, which is then discussed again at the board meeting. **The evaluation of the effectiveness of the committee is conducted in the same manner as the evaluation of the effectiveness of the Board.** By conducting an effectiveness evaluation, it is possible to confirm whether the discussions were sufficient and whether they are linked to the management strategy. [Legal department and board secretariat]
	■ **While external evaluations can ensure objectivity, they do not allow for in-depth discussions. Therefore, external evaluations are conducted every three years, while internal evaluations are conducted in other years.** In the effectiveness evaluation, all directors are asked to express all their thoughts, including those that are difficult to speak out, so that mutual awareness among directors is shared. The PDCA cycle, centered on effectiveness evaluations, has been turning and reform of the board has been progressing thus far. [Board office]
	■ We feel that the evaluation of the effectiveness of the board is a useful tool to improve the board by using the PDCA cycle with annual fixed-point observations. **An important part of the effectiveness evaluation is how the questionnaire items are set up**. By devising a way to highlight the items that are issues, the board will become more aware of them, and as a result, the efforts will be advanced. This is how we were able to promote the delegation of authority and the appointment of female directors. **The results of the evaluation are actively disclosed in an easy-to-understand format using charts and graphs, and are also used in discussions with investors.** [Executive officer]
	■ In order to link to the agenda of the board, we are making efforts in the preparation of the effectiveness evaluation questionnaire to **include questions such as "Are efforts sufficient?" for areas where the secretariat believes that efforts are insufficient in its view.** [Board secretariat]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to engagement with investors (1)

Engagement

- **In addition to the president and CFO, the company's chairman who is an outside director and other outside directors are active in the dialogue.** Although many of our shareholders are overseas investors, we respond to them regardless of the time difference. By reflecting the opinions of investors gathered through these dialogues in the discussions at board meetings and in the actual management of the company, **we have received positive responses, and we feel that the share price reflects this.**
- **Making outside directors a majority does not guarantee an immediate stock price rise. Outside directors will be able to provide advice and discussion based on the real picture of the company with an objective viewpoint, and furthermore, by thoroughly communicating this to investors, the company's reputation will improve.** The company has implemented the comments received from outside directors regarding areas for improvement, even if it has taken some time to do so. I believe that our efforts to explain these reforms to investors and to answer their questions honestly have been well-received.

[Executive officer]

- **Incorporating investor and shareholder thinking and technology into management will improve management performance and increase corporate value.** Engagement with investors who want to work together to improve the quality of management is important, and we have arranged not only major shareholders, but also investors who can provide suggestions for management to meet with the president. As an example, when the president took office, he made the rounds of investors and shareholders to get hints on how to think about the company's challenges and received suggestions that capital productivity is important as a way to look at the company and that companies that handle multiple businesses in different fields should consider factors such as ROIC. The remuneration system also takes into account the opinions of shareholders. Previously, the remuneration system consisted only of salary and short-term bonuses, but we heard opinions that it would be better to introduce medium- to long-term performance-linked bonuses and sustainability indicators, and we have incorporated these suggestions.
- **The president reports to the board on the content of communications with investors.** In addition, other reports from sell-side analysts and stock price trends are reported to all board members when they are released, and investor opinions on earnings announcements are reported at management meetings.
- To encourage investors to evaluate the company, the company engages in a two-way dialogue, including topics related to non-financial values. Disclosure, including the integrated report, is the culmination of this process, and is prepared by considering what to pick up and how to explain it in order to appeal to shareholders. [Board secretariat]

- By repeatedly providing feedback to the top management, the opinions of investors are gradually input into the process and eventually grow into the top management's own awareness, leading to the realization. Matters that are common in the opinions of several investors are of particular importance. [Executive officer]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to engagement with investors (2)

Engagement

- **It seems to me that major investors have come to the view that they should carefully check the policies and management's stance of the companies in which they invest in order to hold shares from a medium to long-term perspective**. As a manager, I would welcome investors who hold shares from a medium to long-term perspective, and I manage the company from a medium to long-term perspective and try to distribute the value created by the company to stakeholders. [Chairman of the board]

- **Companies need to show investors the results that count ultimately.** Investors will demand that a company improve its dignity, including compliance, in order to prove that they are a company that investors can feel comfortable investing in. However, if a company responds to this need alone, no matter how good the strategy is touted or how well governance works, the shares in the company will eventually be sold if the stock price does not rise. At the end of the day, investors demand that companies achieve numbers (results), and this is reasonable. [Chairperson and chairman of the board]

- We communicate regularly with investors. Normally, top management spends a week or two traveling to investors in the US and Europe prior to shareholder meetings, but during the coronavirus pandemic, the engagement was conducted online. **In addition to regular meetings, the company also strives to provide necessary information and exchange opinions in a timely manner, such as by holding a briefing sessions on the mid-term management plan recently to deepen understanding of the plan.**

  [Legal department and board secretariat]

- In the past, the company began meeting with domestic institutional investors after the approval rate for proposals for the appointment of outside directors stagnated. **Through the meetings, we confirmed the views of institutional investors on the independence of outside directors and the criteria for exercising voting rights, and explained the company's view on the independence of outside directors to the contrary. As a result, the approval rate, which had been stagnant, recovered to around 90%**.
- Currently, **the company analyzes the exercise of voting rights immediately after the shareholders' meeting and reports the results of the analysis of voting rights at the board of directors' meeting at the end of the following month**. Based on the results of such analysis, the company regularly holds dialogues between major institutional investors and the company's officers.
- When talking with investors, the director in charge basically meets with investors who have a high percentage of holdings. While referring to the reasons for the exercise of voting rights disclosed by institutional investors, when a institutional investor has exercised its voting rights in opposition, we discuss the reasons for the opposition and what should be done so institutional investor exercise their voting rights in favor of proposals. We also conduct interviews on the future revision of the voting standards. On the other hand, the company explains the progress of the mid-term management plan and the status of governance.
- Not only the director in charge but also the president himself actively engages in dialogue with investors. Prior to the coronavirus pandemic, the president spent a week or two touring Europe and the US, communicating with investors to obtain business references and other suggestions for management. In addition, based on discussions during the re-revision of the Corporate Governance Code in 2021, proposals from institutional investors, and the situation at other companies, **we have had outside directors participate in dialogues with major institutional investors for the past two years, as we believe that their participation in such dialogues will lead to a higher approval rate**. [Legal department]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to engagement with investors (3)

Engagement

- **A team of US investors specializing in each industry asked many pertinent questions, and their analysis based on information on similar rival companies was informative.** They are also under pressure from their clients, the asset owners, and we accept even tough interactions as a matter of course.
- **Despite the various points raised by investors, it is important to continue the dialogue in order to have a constructive discussion. Based on dialogue with investors and other stakeholders and corporate accountability, what a company should do will naturally be determined.** [Chairperson and chairman of the board]

- **Apart from the board, investors who bring outside input are very helpful to management.** Investors who are willing to take a medium to long-term view are important **for the board to pursue medium to long-term initiatives, and increasing the number of such investors is beneficial to the executives.** Investors, too, offer to exchange opinions when they are involved with a company over the long term. [Chairman of the board]

- **While we do interact with analysts in investor relations, we rarely speak with investors because of the scale of our company.** Also, GPIF passive investments are linked to indexes such as women and ESG, and only for market capitalization of 100 billion yen or more, which we do not qualify for so the benefits do not spill over for us. We would like to reform governance, but it is difficult to invest in it, when that may or may not impact the stock price. [Executive officers]

- Despite the fact that the decisions of voting advisory firms have a significant impact on shareholder voting behavior, **some voting advisory firms make very formal decisions.** While the majority of investors are understanding when we directly communicate with them, the voting advisory firms do not respond to our requests for dialogue and continue to issue formal reports, which suggests that improvements are needed, such as strengthening the related system. [Vice president]

- The decisions of voting advisory companies are a formality. We are not swayed by the advisory firms' recommendations, but there are concerns that shareholders will follow such recommendations. [Executive officers]

- **I have the impression that many Japanese institutional investors stick to just the numbers in their evaluations regarding diversity, such as gender, and I believe that this is an issue of accountability**. Although we recognize that the low ratio of women in management positions is an issue when looking just at Japan, it is different when viewed at the global group level, and we are continuing dialogue to ensure that investors understand that the management unit is global.

[Chairperson and chairman of the board]

(Note) Positions are as of the time of the interview

Interviews with companies: Efforts and their effects related to engagement with investors (4)

Engagement

- With regard to engagement with investors, **the company is making efforts to eliminate information asymmetry, and senior management, outside directors and outside *kansayaku* are also present in the company's active engagement in dialogue that aims to increase corporate value.**
- It is difficult to say whether investors are encouraging appropriate risk-taking by companies, since some investors seek only short-term shareholder returns and it depends on the nature of each investor. However, fundamentally, investor feedback has led to an increase in corporate value.

[Board secretariat]

- One of the engagement challenges is that there are **cases where institutional investors own shares via custody and the beneficial shareholders are not known**. I also feel that some investors and voting advisory firms are making voting decisions on a formal basis, without considering the contents of explanations. **The number of passive management investors is increasing, and it is likely that these investors are increasingly relying on the judgment of voting advisory firms and making decisions based on their formal decisions.**

[Board secretariat]

- The evaluation from investors is important to us. When the company was first listed, the founder said, "The stock price is a report card to management." In order to be appreciated by investors, we feel that it is important not only to provide good explanations, **but also to obtain evaluations (indexes, etc.) of the company's efforts from external organizations.**
- We are committed to dialogue with investors because their input is beneficial to the growth of the company. For example, we are aware of the investment trends of investors, such as whether they focus on domestic/overseas stocks, value/growth stocks, and heavy industry, when we conduct dialogue with them. With **investors who have invested with us for a long time**, we have built a relationship of trust and have been able to have smooth dialogue with them.

[Director]

(Note) Positions are as of the time of the interview