1st meeting of the Expert Panel on the Stewardship Code

Material 4

Secretariat Briefing Pack

18 October, 2024

金融庁
Financial Services Agency, the Japanese Government

Contents

Overview of Japan's Stewardship Code

Developed on February 26, 2014
Revised on May 29, 2017
and on March 24, 2020

- The Stewardship Code promotes **institutional investors** to fulfill "Stewardship responsibilities" by improving and fostering the **investee companies' corporate value and sustainable growth** through **constructive engagement**.

Framework

The Code
- Expects each institutional investor to decide whether to sign up the Code or not. The FSA publishes the list of signatories, and thereby encourage more institutional investors to sign up the code.
- Adopts a "**principles-based approach**" instead of a "rule-based approach".
- Adopts the "**comply or explain** (comply with the principles or explain why they are not complied with) **approach** " as opposed to mandatory requirements like laws/regulations.

Principles

Institutional investors should:

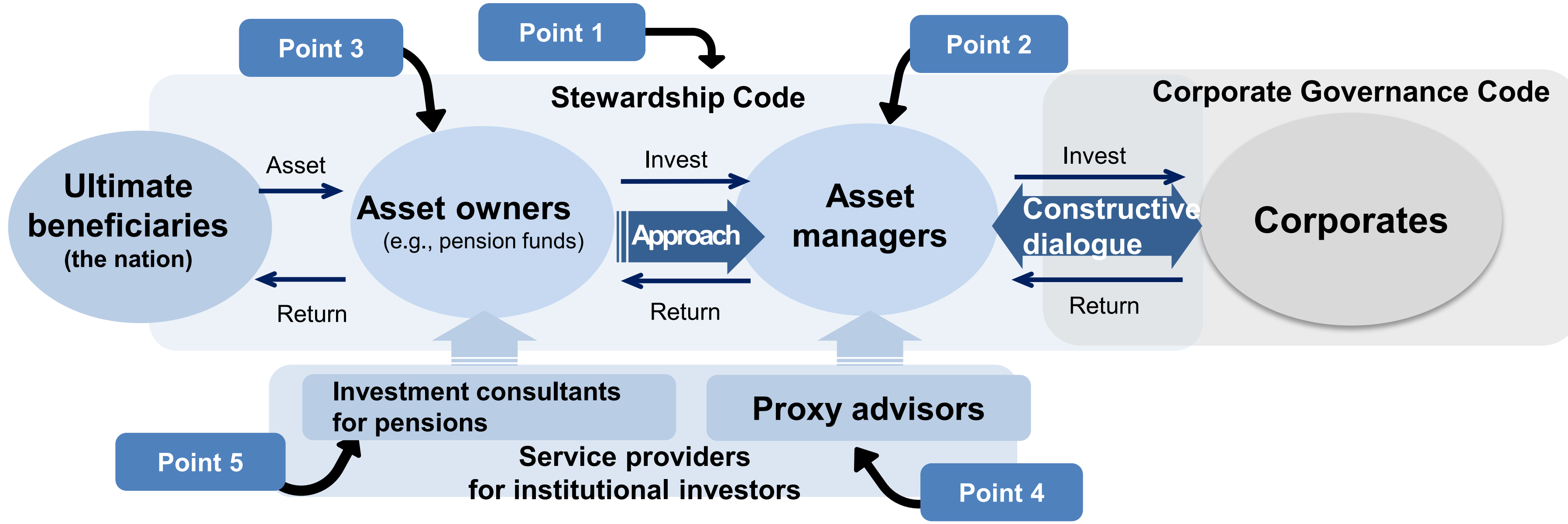
1. Disclose a **clear policy** on how to fulfill their stewardship activities;
2. Properly manage **conflicts of interest**;
3. **Monitor** investee companies;
4. Seek to arrive at an understanding in common with investee companies and solve problems through **engagement**;
5. Have a clear **voting policy** and **disclose voting records**;
6. **Report on stewardship activities** to clients/beneficiaries, and;
7. Have **skills and resources necessary for engagement**.

Service providers for institutional investors should:

8. Endeavor to **provide services appropriately for institutional investors to fulfill their stewardship responsibilities**.

Overview of the revisions to the Japan's Stewardship Code (2020)

☐ To further promote the effectiveness of the corporate governance reform, based on discussions in the Council of Experts on the Stewardship Code (held three times between October-December 2019), Japan's Stewardship Code was revised on March 24, 2020 (second revision).



1. Overall revisions	(1) Consciousness of "medium- to long-term increase of corporate value" (2) Consideration of "sustainability" (medium- to long-term sustainability) (3) Applying to institutional investors holding bond securities
2. Asset managers	・Improvement of disclosure to promote constructive dialogue
3. Asset owners	・Support for stewardship activities of corporate pension funds
4. Proxy advisors	・Improvement of quality of services provided for institutional investors
5. Investment consultants for pensions	・Improvement of quality of services provided for institutional investors

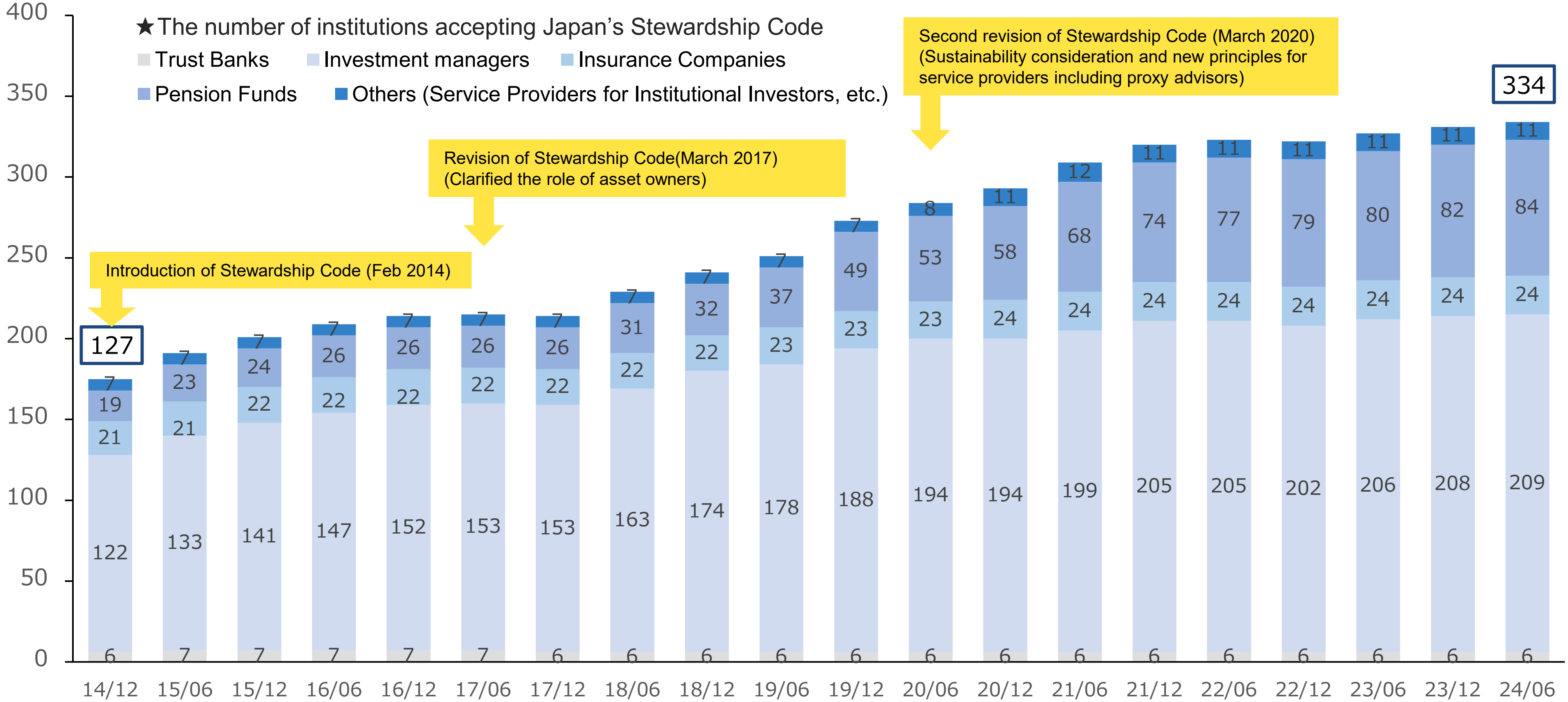
Key revisions to the Japan's Stewardship Code (2020)

1. Overall revisions	⑴ Consciousness towards the medium- to long-term increase of corporate value in stewardship activities ⑵ Consideration of sustainability (medium- to long-term sustainability including ESG factors) ⑶ Applying to other asset classes than listed equities, e.g. bonds, as far as it contributes to carrying out stewardship responsibilities
2. Asset managers	･Asset managers should disclose the reasons of votes on the agendas of investee companies, either "for" or "against", which are considered important from the standpoint of constructive dialogue with investee companies, including those suspected to have conflicts of interest or those which need explanation in light of their voting policy. ･Regarding self-evaluations and stewardship activities including dialogue with companies, it is important to disclose them with consciousness of the sustainable growth of companies and the medium- to long-term increase of corporate value.
3. Asset owners	･Conduct stewardship activities corresponding to their size and capacity, etc.
4. Proxy advisors	･In order to assure accuracy and transparency of proxy recommendations, proxy advisors should: ✓ develop appropriate and sufficient human and operational resources (including setting up a business establishment in Japan) ✓ assure transparency of proxy recommendation process ✓ exchange views actively with companies
5. Investment consultants for pensions	･Develop structures of conflicts of interest management.

Changes in number of institutions accepting Japan's Stewardship Code

- The number of institutions accepting Japan's Stewardship Code has continued to increase since the introduction of the Code on February 2014. 334 institutional investors have accepted the Code as of June 30, 2024.

- 302 institutional investors* have accepted the 2020 revised version of Japan's Stewardship Code as of June 30,2024.(*215 asset managers, 77 pension funds, 10 others)



Source: Prepared by JFSA

Report of the Working Group on Capital Market Regulations and the Asset Management Task Force of the Financial System Council (published on December 12, 2023) (excerpt)

- The Asset Management Task Force of the Financial System Council had discussed efforts for the effective implementation of stewardship activities. Consequently, in a report published in December 2023, the Task Force made recommendations for promoting collective or collaborative engagements.

V. Efforts for the Effective Implementation of Stewardship Activities

Institutional investors, who play a core role in the investment chain, are required to fulfill stewardship responsibilities to promote the increase of corporate value by engaging with companies from a med - to long- term perspective. In that case, **it is necessary to engage with individual companies based on in-depth knowledge of the circumstances of each company, rather than a formalistic or one-size-fits-all response** based simply on uniform numerical criteria or proxy advisor's voting recommendations. In order to provide appropriate incentives for such activities, it is important to share the cost of stewardship activities among the investment chain and establish an environment including policy support.[26]

For the effective implementation of stewardship activities through such engagements, **it is important to encourage institutional investors to make efforts for engagement depending on their status (size, investment policy, etc.) in line with the Stewardship Code**. In order for institutional investors to more actively make such efforts, on the one hand, it is useful to increase the benefits that institutional investors can derive from stewardship activities, and on the other hand, it is also useful to reduce the costs of such activities.[27] In light of this, **it is beneficial for institutional investors to use collective or collaborative engagements actively from the perspective of supplementing qualitative and quantitative resources and reducing costs.**[28]

As an example of specific initiatives in this direction, a certain asset owner is adopting passive investment models focusing on stewardship activities in which the management fee structure is different from that of ordinal passive investment with the aim of improving the overall market through stewardship activities, as well as diversifying and enhancing approaches to stewardship activities. In addition, there are initiatives such as collective or collaborative engagement in which the investor engages with companies in collaboration with other investors and the monitoring of asset managers by multiple asset owners collaboratively.[29] **It is expected that the effective implementation of stewardship activities will further progress as the number of investors implementing these various efforts increases.**[30]

26 In order to be able to promote substantial engagement activities, there was an opinion that consideration should also be advanced on specific measures to realize engagement based on a deep understanding of the actual conditions of companies.

27 There was an opinion that the cost burden, including reporting operations related to stewardship activities, should not be excessive, and that it is necessary to appropriately include such costs in compensation.

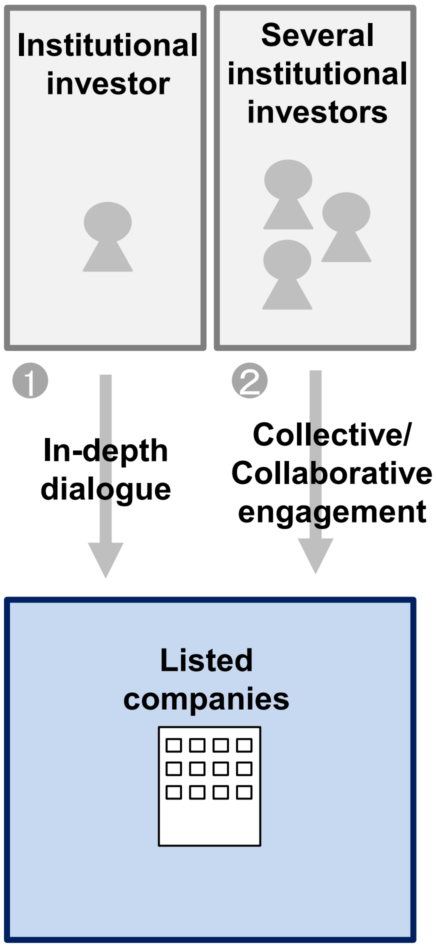
28 There were also opinions that voting advice companies should be required to develop systems based on the Stewardship Code and that the introduction of some sort of discipline should be considered.

29 Regarding the engagement of passive investors, there was an opinion that it should not be forgotten that engagement is not based on a uniform standard of specific numerical values specific to passive investors but is based on a close look at and judgment of the characteristics of individual companies like active investors.

30 There was an opinion that human resource development is also an urgent need for stewardship activities.

Report of the Working Group on Tender Offer Rule and Large Shareholding Reporting Rule of the Financial System Council (published on December 25,2023) (Overview) ~Large Shareholding Reporting Rule~

- For the large shareholding reporting rule, the working group on Tender Offer Rule and Large Shareholding Reporting Rule of the Financial System Council (published on December 25, 2023) recommends as follows.
- Based on the recommendation, the law to amend the Financial Instruments and Exchange Act, including clarification of the scope of the large shareholding reporting rule, was filed.



Large shareholding Reporting Rule

① **In order for passive investors to have in-depth dialogues with companies**, the **rules should be clarified to allow investors to use the special reporting rule,*** if all of the following conditions are satisfied:

- the **purpose** of the engagement **is not directly related to corporate control****
- the **manner** of the engagement **leaves the adoption or refusal up to the company's management**

* See the next page for details of the current rule

** For example, suggested changes regarding dividend policy and capital policy

② **In order to promote collective/collaborative engagement,*** even in cases where institutional investors agree on voting rights, if the investors' **aim of agreement is not to jointly engage in the act of material proposal**, and the agreement is **not for the continuous exercise of voting rights**, they should **not be required to aggregate their ownership ratio as "joint holders"**

* The efforts to engage in dialogue with individual companies in collaboration with other institutional investors

The transparency of beneficial shareholders

In order to efficiently identify the beneficial shareholders(※)

(1) Call on institutional investors to respond when issuer companies ask them about the status of their holdings by clearly stating principles of conduct for institutional investors, and

(2) Make the above responses mandatory under law

※Shareholders who are not a shareholder on the shareholder registry (nominee shareholder) but who have the authority to give instructions on voting rights or the authority to invest in relevant shares

Clarifying “Joint Holders” in relation to the Large Shareholding Reporting Rule

☐ To promote constructive dialogue from a mid- to long-term perspective, the scope of “joint holders” is to be clarified

Issues and policy measures

Issues

- As investors are expected to engage in dialogue with companies based on their in-depth understanding of individual companies, it is important to compensate for the lack of investors’ qualitative and quantitative resources and increase the effectiveness of dialogue by means of collective or collaborative engagement.*

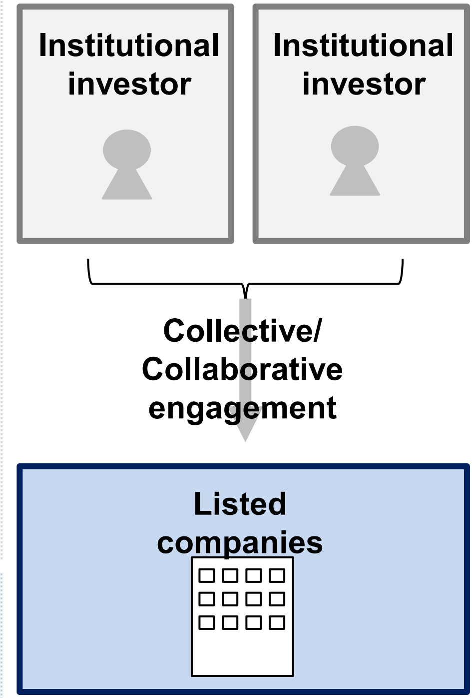
  * Refers to the effort to engage in dialogue with individual companies in collaboration with other institutional investors about specific topics

- However, it is pointed out that joint holders as defined under the large shareholding reporting rule may have room for legal ambiguity and hinder collective or collaborative engagement.

  ※ If two or more investors (Investor A ■%, Investor B □%) fall under the category of "joint holders" (i.e. persons who have agreed to jointly exercise voting rights and other rights as shareholders) and the combined ownership ratio (■%+□%) exceeds 5%, they will be required to submit a large shareholding report.

Policies

- In light of promoting constructive dialogue from a mid- to long-term perspective, the scope of “joint holders” is to be clarified at the level of acts.



Law revision

Clarifying “joint holders” in relation to the Large Shareholding Reporting Rule

■ **Unless two or more investors reach an agreement which would have a material impact on a company’s management,*** they should **not be required to aggregate their ownership ratio as “joint holders”**

* Assuming a case where two or more investors jointly make a proposal that is not directly related to corporate control, such as a change in dividend policies or capital policies

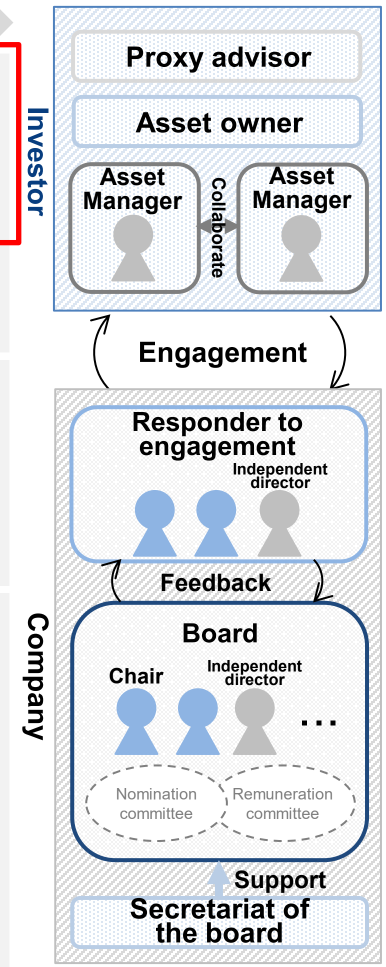
（Ref.）On the other hand, in order to appropriately respond to cases that may threaten the fairness of the capital market, such as cases in which two or more investors stealthily failed to submit reports, a cabinet order is to be revised to deem a joint holder when there are certain external facts, such as an officer concurrent position relationship and a funding relationship.

Action Program for Corporate Governance Reform 2024: Principles into Practice

- Various initiatives are taken based on the "Action Program for Accelerating Corporate Governance Reform" established in April 2023. It is necessary to follow-up on the progress of each measure and consider the future initiatives continuously.

> Going back to the spirit of the Codes, which is to ensure **sustainable corporate growth and increased corporate value over the mid- to long- term**, the following initiatives should be undertaken for putting corporate governance reform **"into practice"** based on self-motivated changes in the mindsets of companies and investors through examining and sharing specific measures.

Issues	Follow up	Future Initiatives
Effective implementation of stewardship activities	✓ The law to amend the Financial Instruments and Exchange Act, including **clarification of the scope of "joint holders" in the large shareholding reporting rule**, was enacted (in May 2024).	✓ Consider **the revision of the Stewardship Code** with the aim of promoting collective/collaborative engagements that contribute to constructive and purposeful dialogues and ensure the transparency of beneficial shareholders. ✓ **Assess compliance with the Stewardship Code** by investors (asset managers, asset owners, proxy advisors, etc.)
Improvement of the effectiveness of the board	✓ Published **"The Basics of Being an Independent Director"** to ensure and improve the quality of independent directors (in January 2024). ✓ The private sector continues to conduct educational activities for directors.	✓ **Share specific examples of efforts**, such as dialogues between independent directors and investors and encouragement for substantive discussions by the secretariats of boards, in order to **promote the implementation of efforts to improve the effectiveness of boards**.
Encouraging the management with an awareness of profit-making and growth	✓ **"Visualized" companies** that make efforts in order to **implement management that is conscious of the cost of capital and stock prices**, including **PBR**, based on the request from the TSE (from January 2024).	✓ **Follow up on the status of each company's initiatives** continuously to encourage them to take substantial measures. In doing so, focus on whether **boards are committed to the initiatives proactively and actively**, whether **specific discussions are conducted during dialogues with investors** and **whether analyses and evaluations are conducted with an awareness of specific outcomes** from the perspective of increasing corporate value over the mid- to long-term occur.

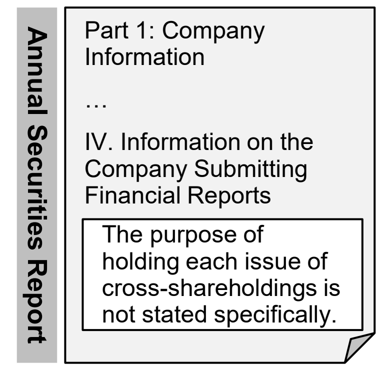


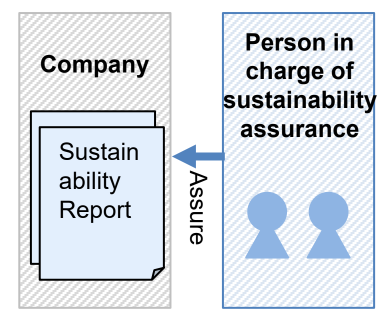
Action Program for Corporate Governance Reform 2024 (cont.)

Issues	Follow up	Future Initiatives
Enhancing the quality of disclosure and promoting dialogues with global investors	✓ **Requested to disclose information about dialogues with investors**, and **published sufficient and insufficient cases of explanations** (in March 2023). ✓ Revised the TSE's Listing Rules toward **mandatory English disclosures** (financial results and timely disclosure information) **from April 2025** (in May2024).	✓ Examine actual situations and advance discussions on the development of an environment, including enhancing the efficiency of disclosures of duplicate information in Annual Securities Reports and Business Reports, that will lead companies to **disclose Annual Securities Reports before general shareholder meetings**, in addition to enhancing **timely disclosures**. ✓ Publish a specific list in order to **"visualize" the group of companies that willingly and actively respond to the expectations of global investors**.
Resolving market environment issues	✓ Requested **the enhancement of information disclosures of quasi-controlled listed companies** (in December 2023). ✓ Published issues and good practices regarding disclosures of **cross-shareholdings** (in March 2024).	✓ Encourage companies to examine their rationale of **cross-shareholdings** in light of the Corporate Governance Code (e.g. whether **appropriate disclosures based on actual situations be made in the Annual Securities Reports**) to avoid a formalistic response.
Encouraging the management with an awareness of sustainability issues	✓ Added metrics on diversity such as **the ratio of women in managerial positions** and **the gender pay gap** in Annual Securities Reports (from the fiscal year ended March 31, 2023). ✓ Published a booklet of companies' good disclosure practices on sustainability issues such as **human capital** (in December 2023). ✓ Amended the TSE's Listing Rules to set **numerical targets for the ratio of female executives at companies (at least 30% by 2030)** (in October 2023).	✓ Discuss **disclosures and assurances of the sustainability-related information while ensuring international comparability**. ✓ **Share specific good examples** such as the awareness of the outcome of increasing corporate value as well as management and dialogues with an awareness of corporate culture.

(The image of a list)
The status of JPX Prime 150 Index Constituent Stocks

Company name	Status of various indicators		Governance items expected by global investors		
	PBR (times)	…	Ratio of Independent Directors (%)	Ratio of female executives (%)	…
A	2.5		37.5	18.2	
B	1.1		41.7	8.3	
C	1.2		44.4	23.1	
D	1.2		44.4	22.2	
E	5.3		33.3	13.3	
F	5.8		66.7	22.2	
G	1.8		60.0	20.0	
H	6.7		40.0	13.3	
I	15.8		37.5	16.7	





Overview of Asset Owner Principles

- While the scope of asset owners is wide and the size of asset owners and the type of funds managed vary, the Government of Japan established **a set of common principles that is useful for asset owners to fulfill the responsibility to manage their assets (fiduciary duties)** in August 2024.
- The Principles adopt a **"comply or explain" approach**. So far, 17 institutions, including 9 public asset owners, have accepted the Principles, which will be followed by the publication of **a unified list of the asset owners who accept the Principles** in January 2025.
- The asset owners who accept the Principles are expected to report their status to their corresponding Ministries.

Principle 1.

Determining the purpose of investment, **investment target and management policy**, which should be reviewed as appropriate.

Principle 2.

Securing talents with sufficient knowledge and experiences, in order to realize the investment purpose and policies.

Principle 3.

Choosing investment methods **for the best interest of beneficiaries**, with **appropriate risk management** and selection of the optimal investment trustee **while managing conflicts of interest**.

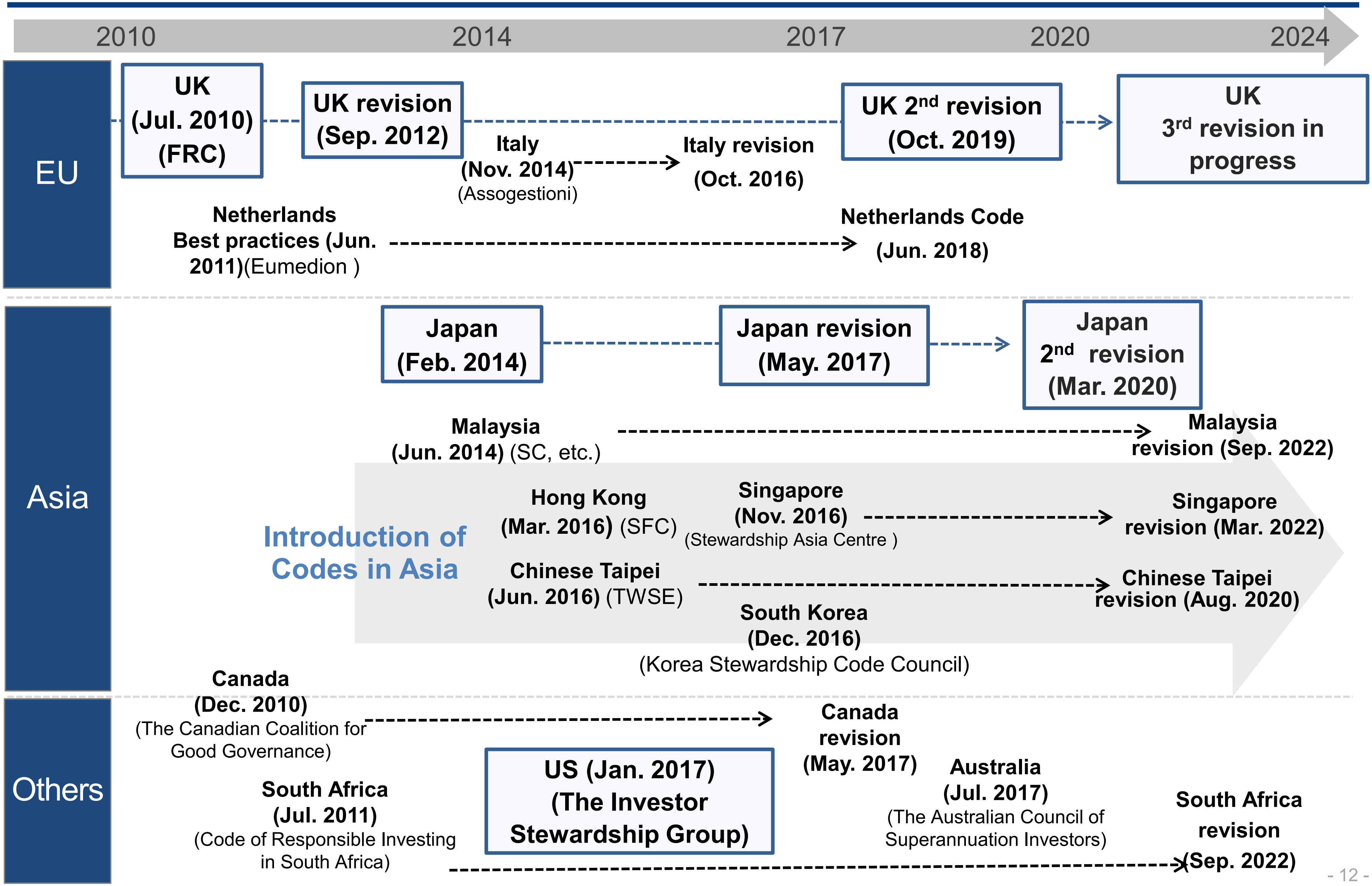
Principle 4.

Providing information of asset under management and engaging in **dialogue with stakeholders**, in order **to fulfill accountability to stakeholders**.

Principle 5.

Encouraging **the sustainable growth of investee companies by conducting stewardship activities**, in order to **achieve the investment targets for beneficiaries**.

Establishment of stewardship codes around the world



Review of the UK Stewardship Code 2020

- The UK FRC has launched a review of its Stewardship Code, including streamlining its principles. The public consultation process will start by the end of 2024 and the revised code will be implemented in 2026. On 22 July 2024, the key themes for the review and interim changes to reduce the reporting burden for signatories was published, based on the results of interviews with stakeholders.

(※) Since the second revision of the code in 2020, the FRC has reviewed each signatory company's reports in detail, as a result of which the reporting burden for institutional investors has been excessive.

Perspectives in the review of the Stewardship Code

- The FRC announced that the review will focus on, amongst other topics, the extent to which the Code:
  - supports long term value creation through appropriate investor-issuer engagement that drives issuers' prospects and performance
  - creates reporting burdens on issuers as well as Code signatories and
  - has led to any unintended consequences, such as short-termism in targets and outlook for issuers.

Key themes for the Stewardship Code review

Purpose	Testing whether the definition of stewardship can lead to the focus of stewardship activity being interpreted as the pursuit of interests beyond long-term value creation further and intending to develop an updated definition of stewardship.
Principles	Exploring a model that would support signatories reporting against the Code in a way that recognizes differences in operating models and how the Principles can better reflect the wide range of assets in which signatories invest, and considering the reporting necessary and looking at ways to streamline the Principles and reporting expectations.
Proxy Advisor	Looking at how the Principles could support improved clarity in reporting on the operation and activities of the different types of service providers, especially, carefully considering how the Service Providers Code might support greater transparency of their activities.
Process	Considering how to reduce reporting, whilst ensuring that information included in the report meets the needs of stakeholders.
Positioning of the Code	Ensuring that the Stewardship Code avoids duplication and considers the impact of multiple domestic regulatory requirements on signatories.

Interim changes to reporting for the Stewardship Code signatories

- Prior to the completion of the review of the code, the UK FRC announced interim changes to reporting against the UK Stewardship Code to help reduce the reporting burden on existing signatories, which are effective for the next application deadline of 31 October 2024, specifically to:
  - Remove the requirement to annually disclose all 'Context' reporting expectations, except for material changes.
  - Remove the requirement to annually disclose against 'Activity' and 'Outcome' reporting expectations for some Principles, except for material updates.
  - Explicitly allow use of content from previous reporting and cross-referencing to such reports, except for material changes.
  - clarify "Outcome" reporting expectations.
  - remind all applicants that collaborative engagement and escalation should be undertaken "where necessary."

Source: Statement: FRC policy update – launch of the UK Stewardship Code 2020 review, 27 February 2024, UK FRC; Key themes for the Stewardship Code 2020 Review, 22 July 2024, UK FRC; Interim Changes to Reporting for Stewardship Code Signatories, 22 July 2024, UK FRC.

Revision of the ICGN Global Stewardship Principles

- The ICGN (International Corporate Governance Network), established in 1995, is an international network on corporate governance and stewardship. In 2016, the ICGN developed the ICGN Global Stewardship Principles as a statement of the ICGN's views on best practices for investors' stewardship responsibilities, policies and processes.
- The Principles have been revised approximately every three years. The latest revision was completed in September 2024. In the revised Principles, superfluous or duplicative language was removed and aspects to reflect recent trends were added.
- Also, in the revised Principles, the chapters were streamlined, from seven to five.

Chapters of the 2020 and 2024 versions

Chapters of the 2020 Principles	Chapters of the revised Principles
1. Internal governance: the foundations for effective stewardship	1. Stewardship commitment (Principles 2, 6, 7 of 2020 version)
2. Developing and implementing stewardship policies	2. Robust governance (Principle 1 of 2020 version)
3. Monitoring and assessing investee companies	3. Monitoring and engagement (Principles 3 and 4 of 2020 version)
4. Engaging companies and investor collaboration	4. Voting and other ownership rights (Principle 5 of 2020 version)
5. Exercising and protecting voting rights	5. Public policy advocacy (Newly established while expanding some Principles)
6. Promoting long term value creation and integration of environmental, social and governance (ESG) factors.	
7. Meaningful transparency, disclosure, and reporting	

The Principles on engagement

3.7 Collaborative engagement

Investors may consider collaborating with other investors to engage with companies and issuers on specific issues, as appropriate. Investors should disclose collaborations undertaken, engagement objectives, time frames, key engagement milestones, and outcomes, as appropriate. Investors should respect 'acting in concert' and market abuse regulations, confidentiality, client interest, and ensure that voting decisions are made individually.

3.8 Reporting on engagement outcomes

Investors should monitor and report progress on the achievement of engagement objectives to their beneficiaries and clients. Disclosures should include how engagement objectives are determined (e.g. by asset type, size of holding, vote-led issues, or geography), the total number of engagement meetings held, any other types of engagement, and themes, where relevant. […]

Source: ICGN Global Stewardship Principles, ICGN

Contents

Survey on stewardship activities (1)

- In order to promote more effective implementation of stewardship activities, JFSA commissioned Mizuho Research & Technologies to conduct a survey of actual stewardship activities by institutional investors, analyze issues, and make recommendations based on these results. From January to March 2023, the survey, in the form of a questionnaire survey of 136 institutional investors and an interview survey of 16 companies, was conducted.
- As a result of the survey, the following issues were pointed out: (1) Lack of resources (human resources and time) for engagement, (2) Insufficient behavioral changes and attitudes at investee companies, (3) Room for improvement in process development (PDCA cycle), (4) Lack of incentives to allocate costs and budgets to activities. In addition, the individual efforts of each asset manager to address these issues were aggregated.

Issues pointed out as a result of the survey

1	Lack of resources (human resources and time) for engagement	• **There is a shortage of human resources with the necessary skills and capabilities to conduct effective stewardship activities** at each asset management firm and in the industry as a whole. • In cases where it is difficult to secure and develop sufficient human resources in-house, it is expected that external knowledge will be utilized through collaboration with other asset managers, including collaborative engagement. However, **the interpretation of "joint holders" under the large shareholding reporting rule is unclear**, and the **burden of the collaboration is concentrated in some asset managers**, so resources may not be sufficiently supplemented through the collaboration. • As a result of the selection of companies for engagement, **small and medium-sized companies tend to be excluded**.
2	Insufficient behavioral changes and attitudes at investee companies	• **Engagement (dialogue) and exercise of voting rights by asset managers may be perceived by companies as formalistic** and may not lead to behavioral changes because companies are not convinced by them. • There is a possibility that in-depth engagement has not been conducted because the interpretation of "act of making important suggestions" is unclear under the large shareholding reporting rule.
3	Room for improvement in process development (PDCA cycle)	• **Asset owners may not have sufficient evaluation and monitoring resources**.
4	Lack of incentives to allocate costs and budgets to activities	• **Stewardship activities by asset managers may not be appropriately reflected in the selection and compensation of asset managers.**

Survey on stewardship activities (2)

- Based on the results of the survey, the following recommendations were made: (1) in order to promote more substantial stewardship activities <u>(i) wide-ranging collaborative efforts among asset managers, (ii) efforts between asset managers and asset owners, (iii) wide-ranging collaborative efforts among asset owners</u> should be promoted; <u>and (2) administrative authorities should appropriately follow up on these efforts</u> so that all concerned parties can work together to improve the effective implementation of stewardship activities.

Initiatives to Resolve Issues

1 Wide-ranging collaborative efforts among asset managers	● Based on the self-assessment of each asset manager's individual issues, it is worth considering **the establishment of a forum** in which asset managers can widely cooperate **to exchange views on the appropriateness of the issues recognized by each asset manager and the effectiveness of efforts to resolve them, and to examine specific measures**. ● As an issue for the whole asset management industry, **an appropriate framework should be established to avoid a situation in which some asset managers are forced to bear an excessive burden** in terms of collaboration with other asset managers, including collaborative engagements. It is also expected that **the asset management industry as a whole will cooperate in efforts to attract new talent**.
2 Efforts between asset managers and asset owners	● **Asset managers should report to asset owners on their own issues and efforts to resolve them**, as well as **appropriately reflecting evaluations received from asset owners in future efforts**. ● **Asset owners should appropriately evaluate the appropriateness of the asset manager's recognition of issues and the effectiveness of efforts to resolve them** based on the above reports, and **appropriately monitor future efforts. It is also expected that the results of evaluation and monitoring will be reflected in the selection of the asset manager and the setting of compensation**.
3 Wide-ranging collaborative efforts among asset owners	● It is important for asset owners to have sufficient knowledge and operational resources for assessment and monitoring. ● **In cases where it is difficult for each asset owner to secure sufficient knowledge and operational resources independently**, it is worth considering **taking measures such as evaluating and monitoring asset managers in collaboration with asset owners who have sufficient knowledge and operational resources** as needed.
4 Follow-up by the administrative authorities	● The administrative authorities should appropriately follow up on the effectiveness of each of the above initiatives and, if necessary, take further measures to promote them. ● **Regarding the ambiguity of the interpretation of "joint holders" and "important suggestions" under the large shareholding reporting rule, efforts should be made to resolve the issues**. At the same time, **the transparency of beneficial shareholders should be improved** so that companies that are not subject to engagement by asset managers can themselves ask for dialogue with asset managers.

Interviews with companies: Situation of engagements and implementation of the corporate governance reform

- With the aim of effective implementation of stewardship activities, the JFSA conducted a series of interviews with individual companies in order to understand the situation of engagements and well-designed improvement of the effectiveness of their boards.
- JFSA selected 12 companies from among those listed on the Tokyo Stock Exchange Prime Market, including those interviewed at the 27th Follow-up Meeting and suggested by Keidanren (Japan Business Federation).

Interviewed companies (in alphabetical order)

- ANA HOLDINGS INC.
- Ebara Corporation
- Inabata & Co., Ltd.
- Kao Corporation
- Kobe Steel, Ltd.
- Mitsui Chemicals, Inc.
- Nitori Holdings Co., Ltd.
- Omron Corporation
- SANYO SHOKAI LTD.
- Sony Group Corporation
- TDK Corporation
- Yamaha Corporation

The JFSA expresses sincere gratitude to all the interviewed companies.

Overview of the interviews with companies (1): situation of engagements

- **Sharing of examples of other companies** that serve as useful references based on the company's situation and continuous engagements by **investors who are familiar with the company's business are likely to lead to constructive dialogue**. Companies welcome any opinions, even if severe, that are considered to contribute to the enhancement of corporate value.
- On the other hand, although such cases are rare, in cases where **investors do not listen to the company's explanation at all** and **communicate their requests one-sidedly, or do not ask additional questions in response to the company's answer and just continue one-sided questions**, it's hard to make two-way communication and develop constructive dialogue.
- Institutional investors need to pay attention again to whether their engagements enhance corporate value and capital efficiency from a mid- to long-term perspective and promote sustainable growth instead of engagements themselves to objects.

Engagements from company's view

Tendency in meaningful engagements

- Investors bring new awareness to companies based on their present situation.
- It is possible to learn about good practices of other companies that can be used as a reference when promoting our own initiatives.
- Continuous dialogue from a mid- to long-term perspective develops into advice tailored to the company's changing circumstances and growth phase.
- Investors well-versed in the business are engaged in dialogue.
- The theme of the dialogue is set according to the company's responders, such as the CEO, CFO, and other people in charge.
- While it is not comfortable to listen, there are indications that will contribute to sustainable growth and increased corporate value over the mid- to long-term.
- Companies can obtain objective assessments based on insights gained from data facts.

Tendency in meaningless engagements

(There are few meaningless engagements, so companies can obtain some kind of awareness and viewpoints in most cases)

- Without considering the present situation of the company, investors pursue the company severely only with idealism.
- There is no concrete advice on how the ideal theory demanded by investors will be realized.
- Discussions progress only by pointing out the appropriateness of formal numerical standards, and there is a lack of explanation of why the standards are necessary.
- Even if companies answer each checklist in the template one by one, there is no additional questions from investors and these simple question-and-answer sessions tend to be continued in a matter-of-fact manner.
- Some investors ask questions from a short-term perspective and persistently demand figures that cannot be disclosed.

Overview of the interviews with companies (2): situation of engagements

- In response to TSE's requests, companies are **changing their behavior and utilizing engagements as a tool for increasing corporate value**.
- In order to meet the expectations of companies, diverse institutional investors also **need to make careful preparations and engage in dialogue in order to fulfill their own roles**.
- In order to make engagements that contribute to the sustainable growth and the enhancement of corporate value over the mid- to long-term, **both sides need to cooperate with each other and continuously confirm the objectives and effects of the dialogue**.

With the aim of improving the engagements			
	Company's Initiatives	Before the dialogue	• By introducing materials before the engagement, we guide investors to read the materials in advance. • We recognize the necessity of engagements more through repeating them and we strengthen the IR department.
		At the time of dialogue	• When CEOs or CFOs engage in dialogue directly, they explain the company's big vision and discuss investors' views towards it. • The board believes that engaging by independent directors only will contribute to promoting investor's understanding, so we provide various opportunities to do so.
		After the dialogue	• We feed back the results of engagements internally, including to the board, in addition, the feedback is provided to investors. • We analyze and disclose issues that investors frequently ask questions about, such as business-specific ROIC and M&A reviews.
	Requests to institutional investors	Before the dialogue	• We would like investors to review our disclosure materials in advance so that we can start the engagement within a limited time under the same viewpoints. • We would like investors to inform us of the engagement agenda in advance so that we can assign appropriate explainers.
		At the time of dialogue	• It is easier to explain and convince management and directors if there are good examples that have led to improved performance and increased corporate value. • Regarding shareholder returns, we would like to discuss whether we should invest in growth business or return to shareholders based on our stage.
		After the dialogue	• We would like to make improvements based on the advice from investors and report them at the next engagement so that we can obtain additional advice. • Since we have to provide overlapping explanations to multiple teams from the same asset management company, we would like investors to share our basic information within the asset management company.

Main opinions voiced in the Japan Corporate Governance Forum (1)

- To accelerate and strengthen corporate governance reforms, JFSA established the Japan Corporate Governance Forum (hereinafter the "JCGF") to hear a wide range of opinions from stakeholders, including overseas investors.
- In JCGF, as in the previous year, while some praised the improvements made in corporate governance, issues were pointed out, such as the effective implementation of stewardship activities, the improvement of the effectiveness of the board, and encouraging the management with an awareness of profit-making and growth.

JCGF event history since April 2023

4th Forum held on May 25, 2023, with the Asian Corporate Governance Association (ACGA)	8th Forum held on October 5, 2023, with ICGN
5th Forum held on June 12, 2023, with U.S. investors, etc.	9th Forum held on July 17, 2024, with ICGN
6th Forum held on June 21, 2023, with the International Corporate Governance Network (ICGN)	10th Forum held on September 27, 2024, with ACGA
7th Forum held on September 28, 2023, with ACGA	11th Forum held on October 3, 2024, with global investors, etc.

General

- We are pleased that the company itself recognized the need for corporate governance reform and is working on it.
- Corporate **transparency** is improving.
- Some companies do not seem to understand the purpose of corporate governance reforms and seem **to consider these reforms formalistic**.
- Many small and medium-sized companies may not be able to follow the action program. While many companies know what they are required to do in corporate governance reforms, **they are not fully convinced about the reforms**.

Effective implementation of stewardship activities

- In order to improve the corporate governance of Japanese companies, it is expected that **Japanese asset managers**, which engage with Japanese companies frequently and do not face a language barrier, **will actively increase pressure on companies**.
- **It is important to make a self-motivated effort to fulfill stewardship responsibilities.**
- It is not realistic to engage with **all investee companies** every year. It is important for investors **to engage in a two- or three-year cycle** to improve the corporate governance of investee companies, and to set and **prioritize the themes of the engagement**.
- It is well received by companies that investors **make proposals to solve issues related to topics in which companies do not have knowledge and experience**. In order to make such proposals, it is important to **utilize collective/collaborative engagement**.

Japan's Stewardship Code (excerpt)

- The Action Program to Implement Corporate Governance Reforms 2024 recommended that:
  - In order to make engagement more effective, the Stewardship Code should be reviewed to **promote collective/collaborative engagements** that contributes to constructive and purposeful dialogue and to **ensure the transparency of beneficial shareholders**, based on the recommendations of the Financial System Council report.

Guidance 4-1.

Institutional investors should endeavor to arrive at an understanding in common[13,14] with investee companies through constructive dialogue[15,16,17] with the aim of enhancing the companies' medium- to long-term value and capital efficiency, and promoting their sustainable growth. In case a risk of possible loss in corporate value is identified through the monitoring of and dialogue with companies, institutional investors should endeavor to arrive at a more in-depth common understanding by requesting further explanation from the companies and to solve the problem.[18]

16 Constructive dialogue between institutional investors and investee companies should not be merely driven by the size of shareholdings. That being said, there are cases when it is appropriate for institutional investors to explain to investee companies how many shares they own/hold.

Guidance 4-5.

In addition to institutional investors engaging with investee companies independently, it would be beneficial for them to engage with investee companies in collaboration with other institutional investors (collaborative engagement) as necessary.[20]

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Collective/collaborative engagement initiatives

- Initiatives for collective/collaborative engagement include those by the Institutional Investors Collective Engagement Forum and the Life Insurance Association of Japan, as well as those by the Investor Forum in the UK.
- **In order to conduct effective stewardship activities** that are appropriate for each investor's situation, **it may be beneficial for investors to utilize these collective/collaborative engagement initiatives**.

	Initiatives in Japan		Initiatives in the U.K.
	Institutional Investors Collective Engagement Forum (IICEF)	**Life Insurance Association of Japan**	**Investor Forum**
Organization Overview	☐ Established in 2017 to support constructive, "purposeful dialogue" (collaborative engagement) conducted with companies through collaboration by institutional investors to contribute to appropriate stewardship activities of institutional investors	☐ Established to promote the sound development and maintain the reliability of the life insurance industry and thereby contribute to the improvement of people's lives ☐ The Association operates a **stewardship activities working group** to help revitalize the stock market and realize a sustainable society	☐ Launched in 2014 with the goal of placing stewardship at the center of investment decision-making by promoting dialogue, creating long-term solutions, and enhancing value
Activities	☐ The Forum operates an **institutional investor collaborative dialogue program** for collaborative engagement • Participating investors discuss issues common to Japanese companies and set the agenda • **The secretariat presides over and facilitates dialogue with the target companies and supports constructive dialogue between the companies and participating investors** • The main agenda includes: ✓ Realizing management that is conscious of cost of capital and stock price ✓ Identifying materiality and disclosing nonfinancial information ✓ Handling proposals with a high rate of opposition at general shareholders' meetings, etc.	☐ **Companies participating in the stewardship activities working group perform collaborative engagement** (commenced in FY2017) • The main agenda includes: ✓ Enhancing shareholder returns ✓ Enhancing disclosure of ESG information ✓ Enhancing disclosure of climate change information, etc.	☐ The Forum has developed a **Collective Engagement Framework that organizes legal risks, etc., and conducts collective engagement in a format that represents the views of participating investors** ☐ Holds events for investor-company dialogue ☐ Shares best practices
Participants	☐ Pension Fund Association, Dai-ichi Life Insurance, Sumitomo Mitsui DS Asset Management, Sumitomo Mitsui Trust Asset Management, Mitsubishi UFJ Trust and Banking Corporation, Meiji Yasuda Asset Management, Resona Asset Management (7 companies)	☐ Asahi Mutual Life Insurance Co., Japan Post Insurance Co., Gibraltar Life Insurance Co., Sumitomo Life Insurance Co., Dai-ichi Life Insurance Co., Taiju Life Insurance Co., Daido Life Insurance Co., Taiyo Life Insurance Co., Nippon Life Insurance Co., Fukoku Mutual Life Insurance Co., Meiji Yasuda Life Insurance Co. (11 companies)	☐ 55 companies (comprising asset owners and asset managers in the UK and abroad)

Sources: compiled by FSA based on websites of relevant initiatives and interviews

Collective/collaborative engagement initiatives

- The UK Stewardship Code and ICGN Global Stewardship Principles refer to collective/collaborative engagement.
- In the UK and EU, the scope of "act in concert" in tender offering rules, that might have discouraged collective/collaborative engagement, was clarified.
- In October 2023 the SEC published a new guidance on the scope of a "group" in the tender offering rules in relation to collective/collaborative engagement.

Soft law on stewardship activities	
UK	- Signatories, where necessary, participate in collaborative engagement to influence issuers. - Signatories should disclose what collaborative engagement they have participated in and why.
ICGN	- Investors may consider collaborating with other investors to engage with companies and issuers on specific issues, as appropriate. - Investors should disclose collaborations undertaken, engagement objectives, time frames, key engagement milestones, and outcomes, as appropriate. - Investors should respect 'acting in concert' and market abuse regulations, confidentiality, client interest, and ensure that voting decisions are made individually

Tender offer and large shareholding reporting rules	
US	- The following actions alone do not constitute a "group." I. Exchanging opinions between shareholdings or collective engagement that is not intended to come to an agreement on concerned action and acquisition, holding or disposal of shares. II. Contacting shareholder proposers. III. Publishing or sharing voting records (including supports for shareholder proposals) that each shareholder has independently determined.
UK	- Exercising voting rights collectively at resolutions of general shareholder meetings on specific matters shall not normally be considered an "act in concert." However, a person shall be considered as acting in concert, if with their supporters, they request a company to take into consideration a proposal to control the board or threaten to request the control of it.
EU	- When shareholders cooperate to engage in any of the activities listed below, that cooperation will not in and of itself lead to a conclusion that the shareholders are acting in concert: i. entering into discussions with each other about possible matters to be raised with the company's board ii. making representations to the company's board about company policies, practices or particular actions that the company might consider taking

Sources: Financial Reporting Council "The UK Stewardship Code 2020"; ICGN "Proposed Revisions to the ICGN Global Stewardship Principles" ; SEC "Modernization of Beneficial Ownership Reporting" Release Nos. 33-11253; 34-98704; File No. S7-06-22 (Oct. 10, 2023); Hidefusa Iida, "The scope of groups and acting in concert," 2014; ESMA "Information on shareholder cooperation and acting in concert under the Takeover Bids Directive" ESMA/2014/677-REV (Jun. 20, 2014; Last update: Jan. 8, 2019)

"Engagement-enhanced passive" managers adopted by GPIF

- GPIF has adopted passive investment models focusing on stewardship activity (**"engagement-enhanced passive"**) ,which includes a compensation structure that differs from regular passive investment, with aims of achieving sustainable growth of overall market through stewardship activities, as well as diversifying and enhancing the approach methods of stewardship activities. Asset managers selected are engaged in stewardship activities according to their own situation, including efficient beta increases by narrowing down companies that have a significant impact on the index, and active involvement by top management.
- In order for effective implementation of stewardship activities, it may be **important to promote responses appropriate to their own situation (size, investment policy, etc.) based on the purpose of the Stewardship Code.**

Characteristics of Engagement through "Engagement-Enhanced Passive" Managers

Asset Management One	✓ Started in 2018. ✓ Engagement on 18 ESG issues is conducted by **ESG analysts and the person in charge of voting rights who have over 20 years' experience, in collaboration with fund managers and analysts from the asset management division**. The engagement activity makes tangible investee companies' challenges, contributing to the improvement of their corporate value.
FIL Investments (Japan)	✓ Started in 2018. ✓ **Aims for efficient enhancement of β by urging companies with a strong impact on indices to make reforms, utilizing knowledge of analysts of active investments.** The agenda of engagement is identified from the perspectives of creating corporate value, and the improvement of profitability and growth potential is pursued by enhancing companies' competitiveness.
Sumitomo Mitsui Trust Asset Management	✓ Started in 2021. ✓ Adopts multi-engagement model in **which the upper management (chairperson or president) actively participates in engagement.** The effects of engagement are maximized for the increase of corporate value by **combining a top-down approach based on ESG materiality and a bottom-up approach from the business operation levels, along with policy engagement**.
Resona Asset Management	✓ Started in 2021. ✓ **Engagement based on the analyses of integrated reports using AI**. Aims to improve the corporate value of investee companies by encouraging disclosure in integrated reports and setting qualitative improvement as interim targets and triggers. At present, the scope has been expanded to the Securities Report and TCFD- based analysis.

Source: compiled by FSA based on GPIF "Stewardship Activity Report for 2022/2023" (March 2023)

Collective/collaborative monitoring initiatives and other Initiatives

- As part of asset owners' initiatives to monitor asset manager, the Pension Fund Association of Japan plans to conduct collective/collaborative monitoring. Some companies are also undertaking engagement support initiatives.

	Collective/Collaborative monitoring initiatives by asset owners	Other Initiatives
	Pension Fund Association	**MFA, Inc.**
Organization Overview	☐ The Association was established as an association of employees' pension funds based on the Employees' Pension Insurance Act, and was reorganized into its current form, Pension Fund Association, in 2005 following amendments to the law ☐ Its main activities: • Pension totalization service • Member support service • Administrative service entrusted by the national government • Management of pension benefit funds	☐ MFA was established in 2022 to serve as an intermediary (agent) that supports the establishment of productive and creative dialogue between the capital markets and companies in the form it should be taking place ☐ Missions: (i) Defining what it means to be "a responsible shareholder" (ii) Establishing an "engagement" model (iii) Creating forums for "fruitful dialog"
Activities	The Association established the Corporate Pension Stewardship Promotion Council to substantiate its stewardship activities in which pension funds are encouraged to participate ☐ **Collaborative monitoring (from summer 2025)** • Survey on asset managers' stewardship activities • Collaborative dialogue with asset managers • Receiving reports from asset managers on their activities and self assessments	☐ **MFA is contracted by institutional investors and others to perform "engagement" on their behalf and provide support for the companies in which they hold shares** ☐ In representing and assisting institutional investors and others, MFA will (i) Engage in dialogue with management and executives (ii) Provide professional services to solve problems (iii) Engage in dialogue with other external stakeholders (financial institutions, etc.)
Participants	☐ As of September, 2023, 67 pension funds participated in the initiative)	☐ Shareholders: Sumitomo Mitsui Trust Bank, CDI Human Capital, Industrial Growth Platform, Misaki Federation, Corporate Directions, Kyoto Bank, Kiraboshi Bank

Source: compiled by FSA based on websites of relevant initiatives and interviews

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Questions for discussion (1)

[Corporate governance reform]

- ☐ The corporate governance reforms in Japan have been aimed to ensure sustainable corporate growth and increased corporate value over the mid- to long- term. What is your view on the roles of the Stewardship code and remaining issues to discuss?

[Effective implementation of stewardship activities]

- ☐ What initiatives are needed towards the effective implementation of stewardship activities by institutional investors?
- ☐ In the context of an increase in passive investments, some suggest that it is important to provide appropriate incentives to institutional investors for stewardship activities and to share the costs among institutional investors. What is your view on how to make engagement more effective?
- ☐ In this regard, what is your view on the following initiatives that institutional investors have worked on ?

  (i) Asset managers: from the perspective of reducing costs, several institutional investors are actively using the framework of collective/collaborative engagement to supplement qualitative and quantitative resources.

  (ii) Asset owners: some asset owners adopted passive investment models focusing on stewardship activities ("engagement-enhanced passive“ managers), which include a compensation structure that differs from regular passive investments, with aims of achieving sustainable growth of the overall market through stewardship activities, as well as diversifying and enhancing approaches to stewardship activities.

  (iii) Asset owners: several asset owners monitor the asset managers in a collective/collaborative manner.

- ☐ Building on the recent publication of the Asset Owner Principles, are there any further measures to be taken, to promote effective stewardship activities by a broader range of entities, for example by ensuring the “comply or explain” approach of the Code?

Questions for discussion (2)

[Transparency of beneficial shareholders]

- In Japan, we do not have a system for companies to identify beneficial shareholders (persons who have the authority to give instructions on voting rights and to invest in shares but are not nominal shareholders).
- Is it useful to improve the transparency of beneficial shareholders, from the perspective of promoting the building of the relationships of trust between companies and institutional investors and making it easy for companies to request dialogues with institutional investors?

[Streamlining the Stewardship Code]

- The texts of the expected revised UK Stewardship Code will be and the revised ICGN Global Stewardship Principles have been streamlined.
- With regard to the Japan Stewardship Code, are there any points that should be streamlined? In particular, are there points where the need for descriptions in the Code has decreased as time has passed since the formulation and revision of the Code, points where there is a sense of duplication due to the history of revision, and points where redundant expressions should be simplified?

[Others]

- In the review of the Japanese Stewardship Code, are there any other important topics to consider?