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Dear Yufu san,

**RE: ICGN preliminary comments on the Japan Corporate Governance Code**

The International Corporate Governance Network (ICGN) would like to take the opportunity to present some preliminary comments on the Japan Corporate Governance Code being drafted by the Financial Services Agency (FSA) and the Tokyo Stock Exchange (TSE). We noted the importance of this in our previous correspondence to the Council of Experts on the exposure draft of the Principles for Responsible Institutional Investors submitted on 8 February 2014.

The ICGN is an investor-led organisation of governance professionals with members including institutional investors based in over 50 countries and collectively responsible for assets under management in excess of US\$18 trillion. Our membership also includes other stakeholders in the field of corporate governance, including company directors and secretaries, professional advisors and academics.

Established in 1995, our mission is to inspire and promote effective standards of corporate governance to advance efficient markets and economies world-wide. This is achieved through influencing public policy on corporate governance issues by engaging with regulators and responding to public consultations, connecting peers through international events, and informing members on emerging issues through guidance and education programmes. For more information about ICGN please visit [www.icgn.org](http://www.icgn.org).

The ICGN would like to offer the following suggestions regarding the content of the Japan Corporate Governance Code which largely draw upon recommendations in the ICGN Global Governance Principles:

**Support of Code development**

The ICGN welcomes the review of the Japan Corporate Governance Code as a positive development for improving the quality of dialogue between companies and investors. Companies and investors have a mutual interest in helping to promote the long term success of the company. It is therefore useful for both parties to have clear guidance regarding their respective roles and responsibilities.

Members of the ICGN are strong supporters of the concepts of flexible application of standards, commonly referred to as comply or explain. In this regard, any set of

principles of governance whether for investors or companies, should be applied with flexibility and understanding of the specific circumstances of individual companies and their markets.

### **Proportion of independent non-executive directors**

We applaud the increasing number of companies in Japan that are voluntarily appointing independent non-executive directors. We recognise the important role that both 'non-executive' and 'independent non-executive' directors play in the effective functioning of a board of directors. We wish to clarify that the term 'independent non-executive directors' refers to directors who are free from any external relationships which may influence the directors' judgment.

The proportions of executive officers, non-executive directors and independent non-executive directors should be determined within national legal, cultural and regulatory frameworks. In the case of Japan, the ICGN supports the position of the Asian Corporate Governance Association which recommends that the minimum number of independent directors should be three or one-third of the board. This is broadly commensurate with the ICGN Global Governance Principles which recommends that the board should comprise a majority of non-executive directors, the majority of whom are independent.

In terms of how the concept of independence is defined the ICGN Global Governance Principles recommends: *"The board should identify in the annual report the names of the directors considered by the board to be independent and who are able to exercise independent judgment free from any external influence. The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination."* (Principle 2.5)

### **Importance of board committees**

We note reference to the 'utilization of voluntary other arrangements' in Principles 4-10, and we would like to emphasise the importance of independent decision-making, particularly as a safe-guard to mitigate managerial self-interest or lack of objectivity in areas such as audit, remuneration and board nomination. In this regard we would refer you to the ICGN Global Governance Principles as follows: *"The board should establish committees to deliberate on issues such as audit, remuneration and nomination. Where the board chooses not to establish such committees, the board should disclose the fact and the procedures it employs to discharge its duties and responsibilities effectively."* (Principle 1.7)

In the context of our comments on board independence made in point 2 above, we would also like to stress the importance of committee independence. The ICGN Global Governance Principles call for key board committees having at least a majority of independent directors.

### **Shareholder engagement**

There is much emphasised by standard-setters and regulators world-wide to enhance communication between companies and investors. This is evident in the amendments to the European Commission Shareholder Rights Directive and in the development of national Responsible Investor codes in a growing number of jurisdictions. In order for dialogue to be truly effective with global investors, it would be helpful for information regarding the general meeting to be published in English

and be made available on the company's website at least one month prior to the meeting taking place.

In terms of vote disclosure, the ICGN Global Governance Principles recommends: *"The board should ensure that equal effect is given to votes whether cast in person or in absentia and all votes should be properly counted and recorded via ballot. The outcome of the vote, the vote instruction (reported separately for, against or abstain) and voting levels for each resolution should be published promptly after the meeting on the company website. If a resolution has been opposed by a significant proportion of votes, the company should explain subsequently what actions were taken to understand and respond to the concerns that led shareholders to vote against management."* (Principle 8.5)

Providing information on a timely basis, and also encouraging companies to hold general meetings in a dispersed fashion – i.e. not all taking place within a short period, thereby making real investor participation impractical – would facilitate more informed investor voting and investment decision-making. In this regard the ICGN recommends the following in terms of the voting decisions made by shareholders: *"Shareholders should seek to reach a clear decision either for or against each resolution or, in specific cases, may wish to abstain. Voting decisions and the rationale taken should be made publicly available in due course and where a vote is contrary to the board's recommended position, should be communicated to the company in advance of the general meeting where possible. Where a shareholder chooses not to vote in specific circumstances, or in particular markets or where holdings are below a certain scale threshold, this should be disclosed to clients or beneficiaries in a clear policy."* (Principle 17.3)

In closing we would like to take the opportunity to congratulate the FSA, together with the TSE, once again in your tremendous efforts to help improve corporate governance in Japan. This helps to strengthen global investor confidence and, together with new principles for investor themselves, will help to foster trust between companies and investor in their mutual interest to protect and generate sustainable company value.

If you would like to discuss any of the points we have raised, please contact me directly or the ICGN Policy Director, George Dallas, by email at [George.dallas@icgn.org](mailto:George.dallas@icgn.org).

Kind regards



Kerrie Waring  
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Copy: Erik Breen, ICGN Board Chairman