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March 26, 2015

Mr. Masaki Shizuka
Director and Senior Executive Officer (Listing)
Tokyo Stock Exchange
2-1, Nihombashi-kabuto-cho,
Chuo-ku, Tokyo 103-8220
Japan

By email and post

Dear Shizuka-san,

ACGA Comments on Development of Listing Rules for the Implementation of the Japan Corporate Governance Code

Thank you for the opportunity to provide comments on the Development of Listing Rules for the Implementation of the Corporate Governance Code (the CG Code) by the Tokyo Stock Exchange (TSE).

The Asian Corporate Governance Association (ACGA) is a not-for-profit association chartered under the laws of Hong Kong. The association is dedicated to assisting companies and markets across Asia in their effort to improve corporate governance practices. In our educational outreach, we are guided by a practical, long-term approach. ACGA's operations are supported by a membership base of institutional investors, such as public pension funds and fund managers, as well as listed Asian companies, law and accounting firms, and universities. ACGA today has more than 100 corporate members, two thirds of which are institutional investors with around US$18 trillion in assets under management globally. They are also significant investors in the Japan market.

ACGA welcomes and supports the Japan CG Code, and we commend the final proposal of the CG Code which is progressive and practical. We look forward to continuing our communications with the Financial Services Agency (FSA) and the TSE on how to enhance the CG Code. We would also like to offer some further suggestions regarding the scope and content of the Listing Rule Amendments for the CG Code:

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1. Differentiated application of the CG Code

Item 1(1) on the Development of Rules for the Implementation of the CG Code stated that Mothers and JASDAQ companies shall be required to explain the reasons for non-compliance with only the "General Principles" of the Code. Given there is inherent flexibility in the concept of "comply or explain" which allows companies to choose what they are in a position to comply and what timeframe (same approach taken for the Japan Stewardship Code implemented last year), it may not be necessary to dispense with applicability of Code principles to these companies. Requiring them to adhere to higher governance standards will benefit them more in the long-term. A different approach in explaining non-compliance with "General Principles" only may also confuse investors in discerning good disclosure.

We are also concerned that the so-called "global trend" in encouraging new industries and "innovative companies" by dispensations with good governance requirements may lead to a "race to the bottom" on quality of companies listed in regional exchanges, an intense debate already in Singapore and Hong Kong.

2. Independence criteria

Item 2 on Revision of Information Disclosure on Independence of Independent Directors/Auditors provides some enhancements on disclosure, "[t]o prevent listed companies from being overly conservative in their judgment" on the independence of directors and auditors. However, as stated in the "Handbook on Practical Issues for Independent Directors/Auditors" (published by the TSE), the current formulation of the independence criteria is whether (i) the director/auditor is likely to be significantly controlled by the management, or (ii) the director/auditor is likely to significantly control the management. We are concerned that this may not be entirely sufficient in providing good disclosure to investors on director and auditor independence, and global investors are keen to see a clear and precise definition of "independence".

The current independence criteria set by the TSE allow for different interpretations in assessing the level of affiliation of non-executive directors. The lack of disclosure requirements for the level of business relationships (such as the percentage of revenue impact from the affiliated entities) means that investors are not able to distinguish one appropriate outsider from another who may pose conflicts of interest. Investors also noticed that companies were starting to come up with their own definitions of independence. For global investors, this would not be conducive to assessing companies on a standardised manner and would disadvantage some companies over others. We urge the TSE to conduct further reviews on the independence criteria for listed companies to bring them into line with international standards, and provide companies with appropriate disclosure guidance.

The TSE may wish to make reference to the New York Stock Exchange rules, where the independence test is that the independent director has "no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organisation that has a relationship with the company)"; and also take into account the approach in the United Kingdom, Singapore, South Africa and Hong Kong, where nine years has been adopted as a benchmark – if a listed company decides that a director with more than nine years' service is still independent, it will be required to

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explain to members why it has reached that conclusion. We would strongly support the TSE in implementing requirements for listed companies to disclose the business relationships and tenure of independent directors in a consistent manner.

3. Language of the Corporate Governance Report

With regards to the requirement in item 1(2) for listed companies to provide reasons for non-compliance in the corporate governance report, there are no references to English translations. As we pointed out to the FSA in our submission of comments to the exposure draft of the CG Code, given the fact that global investors will be very interested, the corporate governance report and the explanations should be made available in English, and on the companies' websites. Supplementary Principle 3.1.2 of the CG Code encourages companies to provide English language disclosures. Further, having the same information available at the same time and with the same level of accuracy is a pre-condition for equal treatment of shareholders, a core principle enshrined by General Principle 1 of the CG Code.

4. Timing and content of the Corporate Governance Report

On the timing of submission of the corporate governance report, we note that the TSE would require companies to submit the corporate governance reports shortly after the AGMs (from 2016). The feedback from our global investor members is that they would welcome the opportunity to review the corporate governance reports well ahead of the AGMs in the current year (as their usefulness for the AGMs in the following year would be limited). Finally, as we have emphasised to the FSA, the TSE should explore conducting a disclosure review within a year (and in the future regularly) to evaluate the quality of the disclosures by listed companies in their corporate governance reports, and whether these disclosures are in line with the spirit and requirements of the CG Code.

Thank you for your attention. We would be pleased to discuss the above issues in further detail.

Yours truly,

Michael Chong

Jamie Allen
Secretary General

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