



日本の企業開示の向上に向けて何をするべきか？ What we should do to improve disclosure in Japan?

Let's discuss and understand the result of CGWatch 2018"

IFRS Digital Reporting Workshop 15th

Date and time : 28 Jan 2019, 18:00-19:30 (Tokyo time)

Japan ranking down to 7th at CG Watch 2018

The result of CG Watch 2016 was published and Japan was ranked down to 7th of 12 countries in Asia. What kind of issues were seen in Japanese companies? There are many types of issues, but today we would like to pick up disclosure issues because this is something we cannot improve without discussing together. How Japanese companies' disclosure (report) look like for foreign investors? What is different from other countries' reports? What kind of information do investors really want to know? Lack of disclosure or lack of activities? Today we hope to discuss and understand these points.

The CG Watch changed the methodology this year. We have published eight reports by 2016. Though previously in five categories, we proposed a new framework in 2017 that we must consider the ecosystem more widely. Among different stakeholders, such as civil society, media, rules, we need a more strict system, so we have reorganized the evaluation categories. The first of the new system is Rule, and the rests are the stakeholder groups. The stakeholders include, first of all, government, regulators, listed companies, investors, accountants/auditors, civil society/media. In addition, we made it easier to compare among different groups. Apart from CLSA (a securities broker which has joint research with ACGA), we surveyed companies by ourselves. We chose 15 from large companies and 10 from Small Caps. 19 High-Level Questions and 74 Sub questions, of which 10 to 11 are about the financial statements. We asked the same number of questions regarding CG, and Sustainability Report, and also board evaluation, Remuneration disclosure. We picked them up from different sectors. Our research is in the same way in all other countries.



Jamie Allen

	Pre-session understanding other Asian countries CG activities	15th workshop in Tokyo
Attendees	16 Investors, sell-side analyst, 1 CPA, 5 Information provider/Media/Researcher, 2 company side, 2 Stock Exchange	26 Investors, 2 sell-side analyst, 7 Information provider/Media/Researcher, 2 CPA, 3 Company side, 1 Academic, 2 Regulator/Accounting setter/Analyst organization. Some oversea attendees via phone

1. Not enough Disclosure on Footnote in English

1.1 What was found by CG Watch research

a) Operating expenses:

Some companies have limited disclosure.

Note: Some companies are good on this point.

b) Receivables/Payables:

Some companies have good disclosure in Form 20F, but not in the consolidated balance sheet under Japanese disclosure rules. There are the same pattern in many companies--that disclosure on footnotes are better in Form 20F. And translated into English as well, whereas securities reports are rarely translated.

Some companies, no breakdown of R/P.

1.2 Case of an IFRS Adopted company.

Some Japanese companies stopped disclosing Footnote for English Financial Statements recently.

This case, Company S stopped disclosing Footnote on Financial Statements for English report, on the year they adopted IFRS. Why? And what happened?

Company S (Before-After IFRS adoption) 2014, J-GAAP. In the securities report, the number of pages for the Consolidated Financial Statements was 48. The English version had 36 pages.

The securities report in 2017, after it adopted IFRS, the number of pages in the consolidated FS is 61.(IFRS FS tends to become longer than J-GAAP FS).

But the English version only has 19 pages

1.1 Not only English, **Yuho** is not released before AGM

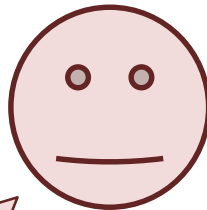


Investor

I am checking the cross-shareholding of banks, but only Yuho has this information. In fact, it is very difficult to collect this information before AGM now. When I discuss the independence of outside directors, I would like to exclude directors from the companies that have cross-holding shares.

But I cannot distinguish them only by the mark "independence". And, in Japan, asset managers have to exercise their voting rights over 1000 companies.

As for the method of obtaining information from companies, I think that there is very detailed information on the IR meeting material, which will be provided to only the investors' community. This is a custom in Japan. And I often compare it with US companies, sometimes it contains more information than US'se.



Investor

As a problem, there are several different reports in Japan at various stages before the AGM (Annual General Meeting). If investors try to understand the company's situation, financial statements and audit information are absolutely necessary but we cannot obtain them before the AGM. There is a Tanshin (the earning digest) and a business report before the AGM, but the information is very limited. Though all necessary information are covered by Yuho (the security report, which is regulated by the Financial Instrument Traded Act), only a very few Japanese companies have issued Yuho before the AGM. In addition, there is English problem. Some of them issue 20 F, but it comes after the AGM. Investors cannot get full picture at the timing of the AGM. Besides, when we discussed "operating expenses" last year, we saw that many insufficient disclosure regarding "Receivable / Payable", "Financial Receivable". Some of them are covered in 20 F, but not in Tanshin (which can be obtained before AGM).



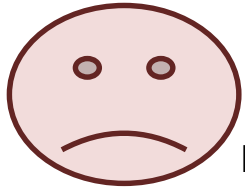
Jamie

All information that analysts can get should be public, it is the "Fair Disclosure". We actually face another problem. We search the CG report at the TSE Website. And go to the company's website to get the business reports. Sometimes I need to get 20 F at EDGAR. As well as taking Yuho at EDINET. That is, we have to go to different sites here and there.

For example, Hong Kong stock exchange provides its database, we can get all the reports, all announcements, documents published by companies in the past 20 years.

It is certainly efficient. Though not all countries are like Hong Kong, our suggestion for corporate reports is that having one database that has everything for all companies.

Can't we postpone AGM after Yuho?



Investor

The important point is we ... No, probably you guys as well, but we want one main report before AGM. Or we can postpone AGM at least one month later? We need one main report that is written about all concerning corporate governance and financial statements which is audited. That is what other Asian countries have. I believe, it is very risky that the audited financial statements come after AGM.



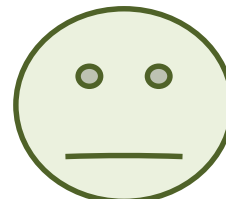
Jamie

Of course, it must be better to submit Yuho before AGM, but it is being said that the Audit cannot be done so quickly. So now the government is considering integrating the business report and Yuho (making those contents the same). It is a compromise, but one of the solution.



Investor

I think that the schedule of AGM can be changed. It is only an issue of a custom. The necessary laws have been revised already. In Japan, more than 3000 companies issue Yuho within 90 days. It must be hard for Audit firms to handle all of them. So I think that the reason why we cannot postpone AGM day with rational reason is just custom.



Auditor

I would like to tell my opinion as Auditor regarding the current issue. First of all, I understand that your opinion "the full set of financial statements should be issued before AGM". I do not think it would be so tough to prepare it before AGM... Maybe we can. But I think that it is important to recognize at the same time, there are separate deadlines by separate laws. If you do not understand this point it will be difficult to understand why separate reports are issued on a separate schedule. When we can understand this point, then our discussion can move on.

It could be easier Audit process and make time for translation?

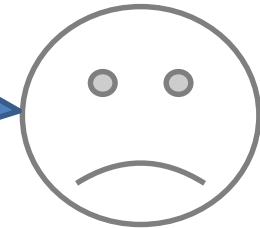


Moderator

We have seen that the Corporate Act and the FITA (Financial Instrument Trading Act) require different things, but the common way in other countries is that if it is listed no longer need to make a report for the Company Act because it will make a report for the Securities Act. Which does not happen in Japan, and what FSA can do now is only to make both the business report and Yuho in the same format...

It is a slightly different argument to postpone the AGM. If we can postpone AGM, whether these reports will be one or not, we can see Yuho before the AGM.

It is also an issue in Japan that we have the audit twice. Once the business report has been audited and auditing for Yuho again, isn't it increasing the cost?
Actually, it must be a big challenge to get agreement on a single report under the one regulation between the Ministry of Justice and FSA. It is logical that to make one report under the FITA, I understand that it is very difficult politically.



Jamie

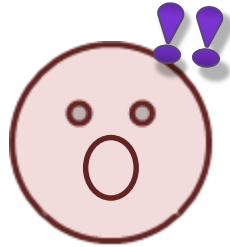


Auditor

Yes, we are auditing two reports. The business report and Yuho are very different. Especially Notes on Financial Statements. So it is not just repetition, we need to broaden the scope of the audit when we see Yuho. I think that if the full set of financial statements comes before the AGM, it would be beneficial to all the parties concerned. It seems to be ideal. But it is difficult from the current situation in Japan under two different legal backgrounds...

I don't think that it is only political, and the purpose of the report is different for each law, so we have to shift the purpose of the report together. I think it is a serious challenge.

Were not aware, only English FS notes is shorter



Investor



Moderator

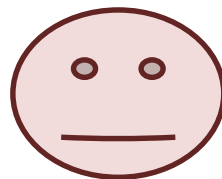
In the case of Agenda 1.2, some companies do not make complete English translation version recently, especially cutting some footnotes. Company S, in 2014 applying J-GAAP, English version report had 36 pages for the consolidated financial statements, though this is shorter than the 48 pages of relevant part of Yuho. The issue happened when S applied IFRS in 2017. Normally the number of pages of Financial Statements increased compared to J-GAAP, it became 61 pages. But the English version had only 19 pages. Around 2017, it seems that some companies cut the footnotes of the financial statements for the English version. Did you notice this?

I have not noticed such issues, but it is intriguing...

No, I thought that Japanese-to-English translations were basically same. So I thought that the amount of information must be the same... At least, if it is an official financial statements. Of course, on the WEB site, there are more Japanese information, I thought... but...



Investor
In Netherland



Investor

English disclosure is also important. But I think that the company should disclose in at least one language with quality and sufficient amount of information. Since Japanese is a local language, so I hope that the company make more disclosure than accurate translation.



Investor

Perhaps, first of all, we need at least in one language timely, a full set of audited financial statements before AGM. Then ideally, if the company wants to head more to international markets, they should disclose the equivalent amount to Japanese. Again, you should start to put all the information on one site, easy to find and timely. Before the voting.

2. Disclosure regarding corporate governance information

2.1 What was found by CG Watch Research? (Jamie)

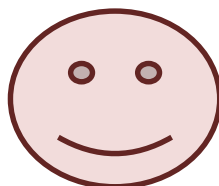
As with other countries, Japanese companies are making reports that look better, with a lot of energy and creativity about the ESG sustainability report. But they do not pay too much power on the CG report. Taking the cheapest option, creating a minimum report.

At the survey in 2016, we pointed out that there is a problem in disclosing information on corporate governance. Partly in the CG report, some in the business report, some in the sustainability report, and some in the Yuho. Information is dispersed like that. This time, we watched a bit more detail. Board Report, Committee's Reports, Board Evaluation, Board / Diversity Statement, Disclosure about Director's Skills ... In general, I think that Japan is not so different from other markets. But the committee's report is very limited. Which companies have Audit Committee, or Kansayaku. There is only very little information on what they have done. Even if there is a nomination committee and remuneration committee, it is the same situation. The board diversity statements are also limited, and skill metrics are so. There is explanation about each board member, but information on background and skills are limited. Some companies are doing good disclosure, for example, some board members' statements, the contributions of each board member, etc..

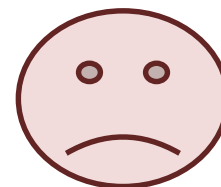
But many companies did not. There are few descriptions of Remuneration policy, so information on how much they paid or how they measured the results is limited. Regarding board evaluation, "Evaluated", "The board was very effective". It is a simple explanation like "The performance of the board was excellent." Board training also says "Boards took training" and it does not say what they did.

Japan has just introduced a CG code several years ago and many companies have not yet established a nomination committee and remuneration committee, in which case there is no Nomination Policy nor Remuneration Policy. So they don't have what they can report. I think that it will increase little by little, it is expected two or three years later.

I think that this is a bit of a structural problem, as for many companies still CEOs choose the next CEO, even if there is a nomination committee. This is a reason why they can not disclose, and as same as remuneration committee. Although some companies are different, many companies still are not performance-based. This is not a matter of disclosure, it is a matter of culture and structure.



Investor



Investor
In Singapore

2. Disclosure the CG report

2.2 What happened the CG report after CG code was revised (Toyo Keizai)

We summarized the cases in which companies changed to "explain" after the revision. Today, will introduce top 5 (number of change).

First is Principle 1-4, so-called "Cross-shareholding". The previous version just said "let it reduce", but revision version added, "Disclose the verification". I think that it worked. The number of "explanation" increased. In other sections where expressions such as "please disclose" are firmly put in place, the number of "explanation" is also increasing, I think that it is quite effective to insert just one word "disclose" to make company understand the code requirements correctly.

Next, 4-8, the Independent Outside Director, because the term "by voluntary judgment" was removed and it became a more mandatory expression. In addition, there is also the figure "1/3", so in case that company doesn't have one, they are no longer able to make an unclear report. I think that it is effective to specify the numerical standard.

Next 3-1, the selection and dismissal of the officers, I think that although many companies have a procedure for appointment, they didn't have a procedure for dismissal.

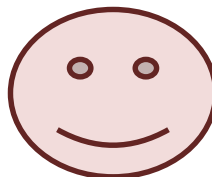
4-11-3 and 4-11-1 are both elementary principles, I think that diversity including gender and internationality has been added to 4-11 and it influenced that women and foreign officers are included. I think that the number of "explanation" has increased over the whole, but there are many template type of description at the same time. Of course some companies are making good disclosure, for example, explaining how much the number of shares is reduced, how much is now on the BS, explaining the numbers... but not many. There are overwhelmingly many companies that are not so, my concern is that the companies make template type explanation about what they do not want to do, and they won't do it actually. Such kind of loopholes solution might be created...



Jamie

About 1-4, although I feel that these descriptions are not much different in English, (before and revised) Maybe I should also read the Japanese version (lol)

I think that this is a little strong, "its own judgment" looks the same way, but maybe the translation of "Judgment" is something different??



I agree the increasing "explanation" is important. Because it is better than "not to comply" or "no explanation". The problem is that in Asia the phrase "Comply or Explain", basically it is comply. For example, the Singapore regulator said that "comply is better".

When regulator says "comply or Explain", they supposed to say "you have a choice". In fact, it is not so, and it is easy for the company to say "we comply". And when the regulator surveyed, "It is wonderful 90% comply". But as the market message, not easier to "comply", but "you should think".



Jamie

3. Audit issues for future Key Audit Matters

Recently, Key Audit Matters (KAM) has been discussed many times in Asia. I think this is a positive step. A survey was conducted on introducing Key Audit Matters in Singapore and Malaysia, but it is generally welcomed by investors that it increases information that can be asked to companies at the engagement. But sometimes the only obvious issues to be easily written and made investors disappointed.

A typical (revised) audit report contains KAM and audit procedures. As a reality, many investors understand that the audit procedure is considered important. However, some investors look at this and asked, "Did you discover any problems in these audit processes during the audit? If so, share them with investors." This part is not usually written, the auditor raises concern as KAM, and say "it is Unqualified opinion". So some investors say there is not enough information in the audit report .

Perhaps in Japan, KAM will be disclosed only in Japanese, when it will be introduced. As we discussed in the first half today, I think it should be clearly written in English so that many investors can share it.

In the absence of the Audit Committee, this is an interesting issue. Clearly, I think the Kansayaku is a limited authority to the board. He/she should report the interaction with the independent auditor to the board, but really, in truth, when introducing KAM, I think the regulator should force the company to have the audit committee. Otherwise, it is difficult to discuss what is KAM at the earliest stage with management. And that audit committee should be independent. KAM will give the auditor the freedom to disclose what they really wanted to disclose. When KAM was introduced in other Asian countries a few years ago, I heard opinions that it would be a boilerplate soon. Just repeating the same KAMs every year. The airline would write only the hedge of the fuel price as KAM. There are truly some reports that have already been boilerplate. Even so, investors should read them and give feedback to companies and auditors.



Jamie



KAM is said that it is useful in most markets. However, it is not good for investors to focus only on KAM. The auditor might be unable to write investor's doubts about the material accuracy of the financial statements which management would be upset. What is important is how disclosure is made in the company's annual report. It is good to use KAM as a tool to judge management's assumption and estimate. CEOs should understand KAM a couple of months before it would be published and improve company report earlier. I think that KAM is a platform for auditors and management to think about disclosure.

Yuho is the most important



Not UFO, Yuho

KAM is a tool to explain what the auditor did. It describes what kind of things have been done in the audit, what was material, and so on. So this is an accountability tool. We, auditors, will also do our best to implement KAM. However, not everything can be seen by KAM, it should be positioned within the relationship of disclosed information from the company, as a whole. FSA is trying to extend information disclosure in Yuho. It includes the explanation of what the Audit committee discussed as important auditing issues related to KAM, and explanation on how the management responded to them based on their responsibilities.

Although such disclosure is a big challenge for management and the Audit Committee, I believe that by effectively functioning as a whole, company disclosure in Japan will be greatly improved.



Auditor

We are really waiting for KAM's introduction, but the problem is its timing. Because again, it will come out after AGM, we can use the information a year later... this is the problem.



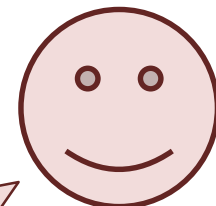
Investor

I think, KAM should be information for investors, so it should be come out before AGM



Investor

In the past, I think that the audit was a black box. In many countries companies already have allowed auditors to speak at shareholders meetings. In the Netherlands for example, the auditor comes to the AGM to announce the opening statement and answers questions from the shareholders. I think that debating openly with investors is a necessary direction in the future and it is very helpful.



Investor
In Netherland

Conclusion “What we should do?”

- Investors need timely, quality and sufficient amount of disclosure at least in one language. We should realize that the main report containing the topics concerning corporate governance and the audited financial statements with full footnotes is needed before AGM.
- Not like other Asian countries, the audited financial statements with footnotes is not disclosed before AGM, it is a risk. Even if KAM is introduced, it is still disclosed after AGM, it is not very useful.
- Also, in Japan, it should be a burden to conduct audit twice. It may be a solution to postpone AGM at least a month.
- The information analysts can obtain should be all public from the perspective of Fair Disclosure. And it should not be on different sites like it is now. (For example, Hong Kong Stock Exchange has a database and store all the reports for the companies. All reports, all announcements, and documents announced by companies in the past 20 years are able to be acquired) Won't Japan have a database that keeps all the reports of all companies which have been issued in past?
- As a next step, if the company wants to go to the international market, issue Yuho and equivalent English information before AGM. KAM should also be disclosed in English if possible.