

January 21, 2025  
Institutional Investors Collective Engagement Forum

## **Recommendations for Measures to Enhance the Effectiveness of Reducing Cross Shareholdings**

We, Institutional Investors Collective Engagement Forum (IICEF), commenced collective engagement with companies regarding their policies on cross shareholdings in the spring of 2019, and in September 2020, published a letter summarizing investors' common views (Refer to Attachment 1). Furthermore, from the autumn of 2022, we have conducted hearings with companies believed to be good examples that are advancing the reduction of cross-shareholdings (Refer to Attachment 2).

Investors welcome the recent materialization of movements to reduce cross shareholdings across a wide range of industries and companies, including the automotive and insurance industries. On the other hand, many companies still hold a significant amount of cross shareholdings. Additionally, in the course of our hearings, we heard many voices indicating that even if a company intends to reduce its cross-shareholdings, actual reduction is not easy due to relationships with business partners. This theme is not yet "a closed chapter"; rather, we consider it a challenge where a "bedrock" stands in the way. The remaining issues cannot be overlooked, and investors still have concerns and a sense of crisis.

Therefore, based on our experience in dialogue with companies thus far, the Forum has decided to compile recommendations for further promoting the reduction of cross-shareholdings. The contents of the recommendations are as follows:

\*\*\*

### ■ Strengthening the Discipline of Corporate Governance Code (CG Code) Principle 1-4

- Regarding CG Code Principle 1-4, "Listed Companies should establish and disclose specific standards with respect to the voting rights as to their cross-shareholdings, and vote in accordance with the standards.," we believe that consideration should be given to mandating the disclosure of individual voting results, not limited to standards disclosure.
- We believe it should be explicitly stated, as CG Code Principle 1-4 or its Supplementary Principle, that "it is inappropriate to make shareholding a condition for business transactions".
- Regarding CG Code Supplementary Principle 1-4①, "When cross-shareholders indicate their intention to sell their shares, companies should not hinder the sale of the cross-held shares by, for instance, implying a possible reduction of business transactions.," we believe that policies for dealing with cases where a counterparty indicates an intention to sell should be an item for disclosure in the Corporate Governance Report.
- In relation to the above, we believe it would also be beneficial for the authorities to re-disseminate the view on cross-shareholdings that was indicated in the Japan Fair Trade Commission's "Guidelines on Trade Practices" (before the 2017 revision).
  - The "Guidelines" before the 2017 revision (hereinafter "Guidelines") clearly stated that the following acts could be problematic under the Antimonopoly Act:
    - Unjustly refusing transactions with businesses that do not own their shares.
    - A business in a dominant bargaining position using that position to conduct transactions with a supplier that owns its shares on the condition that the supplier does not dispose of its shares.

- When the Guidelines were revised in 2017, these descriptions were deleted from the Guidelines, as voices were confirmed from hearings with daily necessity manufacturers, wholesalers, and retailers, etc., indicating that the influence of cross-shareholdings on transactions had diminished. However, from the corporate hearings in Attachment 2, it is strongly inferred that these acts are widely practiced in the construction, real estate, and railway industries, etc.. It should still be the case that the conclusion that these acts can be problematic under the Antimonopoly Act remains unchanged, and it is strongly expected that the authorities will re-disseminate information on the Antimonopoly Act issues related to cross-shareholdings.

■ Clarification of Stewardship Responsibilities for Shareholdings

- We believe that even operating companies and financial institutions, considering the large proportion of their shareholdings in TSE-listed companies, should be required by the CG Code to take actions similar to those required by the Stewardship Code if they hold shares of other listed companies, whether for policy purposes or pure investment purposes.

■ Strengthening Disclosure in Annual Securities Reports

- The past five years' reduction performance of cross- shareholdings, and if there is a reduction policy, its policy and target (level/timeframe), or if there is no reduction policy, the reason for it, should be disclosure items in the Annual Securities Report. At that time, it is desirable that the timeframe for the reduction policy should set a certain deadline, such as 3-5 years, and the target level should be shown on a market value basis, not on an acquisition cost basis. Furthermore, it is desirable that voting results, and whether or not the company has approached the counterparty regarding a sale, etc., should also be disclosure items. When the reason for continuing cross-shareholdings is disclosed as maintaining business relationships, etc., it should be required to disclose specific verification details, such as the indicators referenced, as "content of verification by the board of directors, etc.".
- Companies should disclose the amount including deemed shareholdings when disclosing the above reduction targets and reduction performance.
- Regarding "deemed shareholdings," currently, information on individual issues with the highest holding amounts is disclosed separately from cross-shareholdings, but the total number of issues for deemed shareholdings and their book value are not disclosed, nor are they included in the total number of issues and total book value of cross-shareholdings. Since cases are observed where companies disclose "reduced cross-shareholdings" by contributing cross-shareholdings to retirement benefit trusts, we believe that as long as the company retains the right to instruct the exercise of voting rights, these should be treated as cross-shareholdings, and the total number of issues for deemed shareholdings and their book value should also be subject to disclosure.
- Among cross-shareholdings, some are held for purposes such as capital/business alliances with other companies or supporting/fostering venture companies. However, the quantitative disclosure of their specific holding purpose and holding effects is not necessarily sufficient. We believe that the authorities should consider undertaking necessary efforts to encourage listed companies to provide enhanced disclosure, understanding the significance of these disclosure items.
- The status of cross-shareholdings is currently required to be stated on a non-consolidated basis, except in the case of holding companies. From an investor's perspective, limiting the disclosure of cross-shareholdings to a non-consolidated basis is not deemed rational. We believe that the disclosure of cross-shareholdings should, in principle, be on a consolidated basis regardless of whether the company is a holding company, and if the practical burden is large due to a huge number of consolidated subsidiaries, changes such as disclosing consolidated subsidiaries should be considered.

- Given the current situation where many companies submit their Annual Securities Reports after their general shareholders' meetings, making it difficult to exercise voting rights considering the cross-shareholdings status at the latest fiscal year-end, we believe that disclosure equivalent to the " Cross-Shareholdings Status" in the Annual Securities Report should be required in the notice of convocation.
- Regarding the Reclassification from Cross-Shareholdings to "Pure Investment"
- Generally, from an investor's perspective, there is no rational reason for an operating company to invest in listed equities. Using shareholders' capital for equity management business that is not core business is not rational from the perspective of capital efficiency and means that management is not fulfilling its fiduciary duty to shareholders. Operating companies that reclassify to pure investment should provide sufficient explanation and disclosure regarding the reasons, policies, and systems for equity management, such as why they conduct equity management and under what system. We also believe they should take actions similar to those required by the Stewardship Code.
  - When financial institutions conduct equity investment as part of their core asset management, they should explain that it is appropriately managed from perspectives such as ALM (Asset Liability Management), apply the Stewardship Code, and disclose their voting policy and voting results.
  - Under current disclosure rules, in the first year of reclassification to pure investment, the number of shares held per individual issue is disclosed, but from the second year onwards, the status of individual issue holdings is no longer disclosed. We believe that for reclassifications predicated on sale, disclosure equivalent to cross-shareholdings should be required until the sale is completed, and for reclassifications due to other reasons, for at least 5 years after the reclassification.
  - Current disclosure regulations and notes for completion define "pure investment" within "investment securities" as shares "held solely for the purpose of profiting from fluctuations in stock value or dividends related to shares". However, such "pure investment" might be considered to fall under "trading securities" recorded as current assets under financial instruments accounting standards, rather than "investment securities" recorded as non-current assets.
  - Companies that reclassify cross-shareholdings as "pure investment" should appropriately manage these, including recording them as trading securities among current assets. Even when classified as "pure investment" within "investment securities," as indicated in the practical guidelines for financial instruments accounting, it is desirable to clarify in the articles of incorporation that the company engages in the business of buying and selling shares (securities) and to establish an independent specialized department capable of routinely executing trading operations. We believe that the authorities should clearly state in the Disclosure Regulations and Corporate Governance Code, etc., that this view also applies to "pure investment" within "investment securities". (*This section refers to the views of Professor Shoichi Tsuburaya, Hitotsubashi University, in his lecture material at the Japan Corporate Governance Network on November 11, 2024.*)
- Issues with Business Partner Stock Ownership Plans
- Although the Japan Securities Dealers Association's "Guidelines on Stock Ownership Systems," which serve as operational guidelines for business partner stock ownership plans, stipulate the prevention of abuse of superior bargaining position and that shareholding should not be a condition for transactions, and the holding ratio to the issuing company is low, and the contribution amount per participating business partner is not large, and non-uniform exercise of voting rights is also possible, their purpose is stated as "contributing to the promotion of friendly relations among parties involved through the acquisition of target shares by business partners," making them cross-shareholdings. From an investor's

perspective, forming good inter-company relationships should be achieved through deepened collaboration under fair transactions, not through shareholdings, and business partner stock ownership associations, one of Japan's long-standing customs, are based on the old idea of creating stable shareholders, similar to cross-shareholdings, and involve certain burdens on business partners, which are underlying issues.

- Given these perspectives, the implementing company should listen to the opinions of business partners participating in the business partner stock ownership plan and ascertain the actual situation, and then, in light of the policy to reduce cross-shareholdings, consider whether to continue and disclose the results.

■ Strengthening Industry-Wide Initiatives

- In industries such as construction, real estate, and railway, there are companies that have a dilemma where they want to reduce holdings but cannot commit to it due to reasons such as "unawareness of the movements of competitors" or "a field to write the number of shares held in tender application documents" (Refer to Attachment 2). In view of these problems, we believe that the government and industry associations should formulate and publish policies to promote reduction as an industry, or codes of conduct stating that there will be no review of order volumes due to the reduction of cross-shareholdings, etc..

■ Strengthening the Supervisory System

- A "suggestion box" should be established where companies that have offered to sell cross-shareholdings can report to supervisory authorities if they experience actions such as business disadvantages suggested by business partners. The authorities, under a strict confidentiality management system, should conduct hearings with reported companies and build a system that can appropriately cooperate with the Japan Fair Trade Commission based on the content.

■ Providing Incentives for Sale

- For the purpose of promoting the sale of cross-shareholdings, consideration could be given to introducing tax exemption measures limited to cases where the proceeds from the sale of policy shareholdings are utilized for capital investment, research and development, climate change countermeasures, etc..

End of Document

Contact information

Institutional Investors Collective Engagement Forum

Directors in charge: Yuki Kimura, Chairman; Naomi Yamazaki, Administration Manager; and

Ryusuke Ohori, Hiromitsu Kamata, and Daiji Ozawa, Executive Director

Address: Tokyo Entre Salon, Shinmaki-chou Building Annex 1, 3-2-14, Nihonbashi, Chuo-ku, Tokyo

103-0027 JAPAN

E-mail: [info@iiccf.jp](mailto:info@iiccf.jp)