

Explanatory Memorandum on the Audit & Supervisory Board Members

(The companies without Audit & Supervisory Board)

Japan Audit & Supervisory Board Members Association
(JASBA)

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1 Corporate Governance in Japan (two different systems)

In Japan, most of companies limited by shares must adopt either of the following two governance systems, namely the “Companies with Audit & Supervisory Board Members” or the “Companies with the Three Committees”.

※ 97.8% of the companies listed on the Tokyo Stock Exchange (2,275 companies in total) are Companies with Audit & Supervisory Board Members (as of September 2012)

The Companies with Audit & Supervisory Board Members

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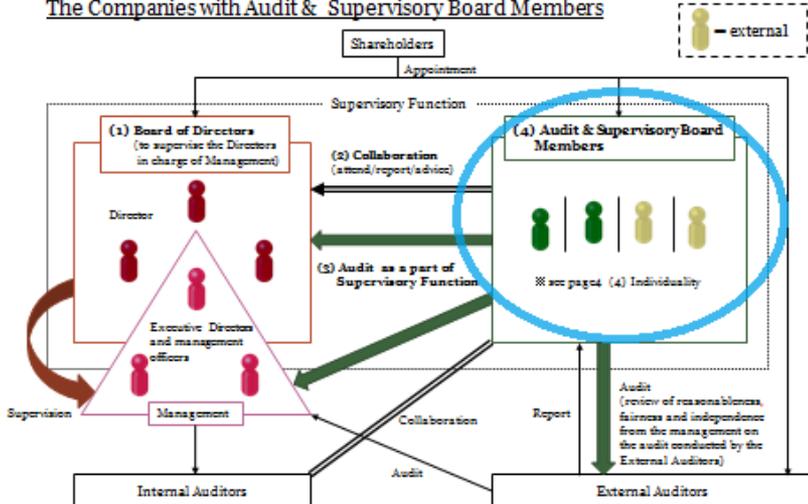
The Companies with the Three Committees

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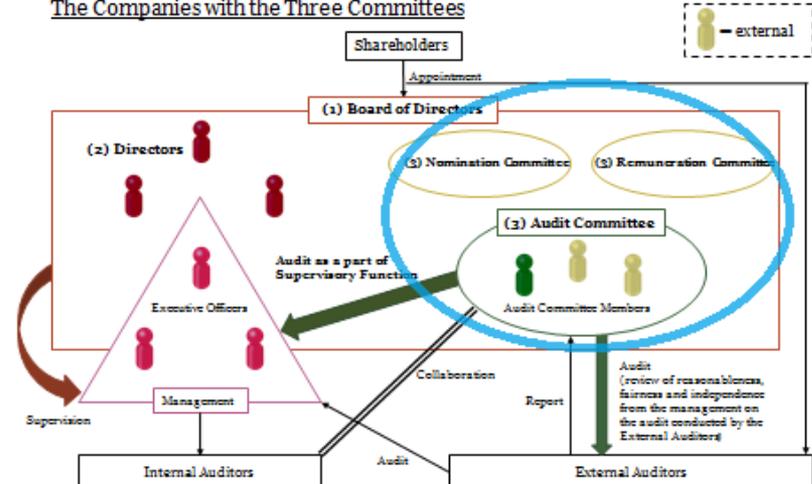
1 Corporate Governance in Japan (two different systems)

The Companies with Audit & Supervisory Board Members



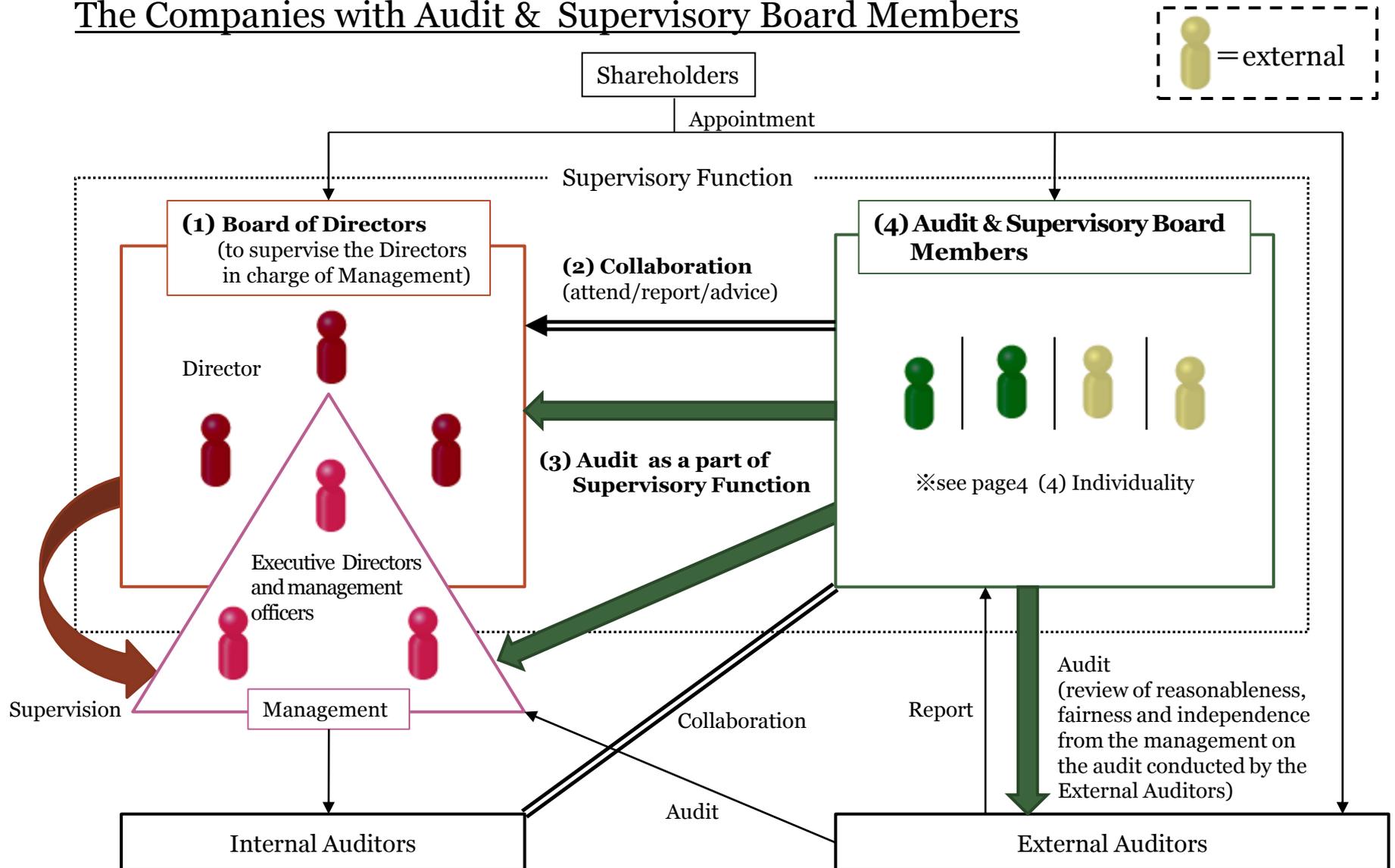
1 Corporate Governance in Japan (two different systems)

The Companies with the Three Committees



1 Corporate Governance in Japan (two different systems)

The Companies with Audit & Supervisory Board Members



1 Corporate Governance in Japan (two different systems)

Features of the Companies with Audit & Supervisory Board Members

(1) Board of Directors

Each Director can act as a member of management as well as a member of the Board of Directors.

(2) Independence and Collaboration

Each Audit & Supervisory Board Member (hereinafter referred to as the “Member”) is appointed directly by the shareholders. Each member is independent not only of management but of the Board of Directors though it is required to collaborate with the Board of Directors in performing its supervisory functions over management.

(3) Major Supervisory Function

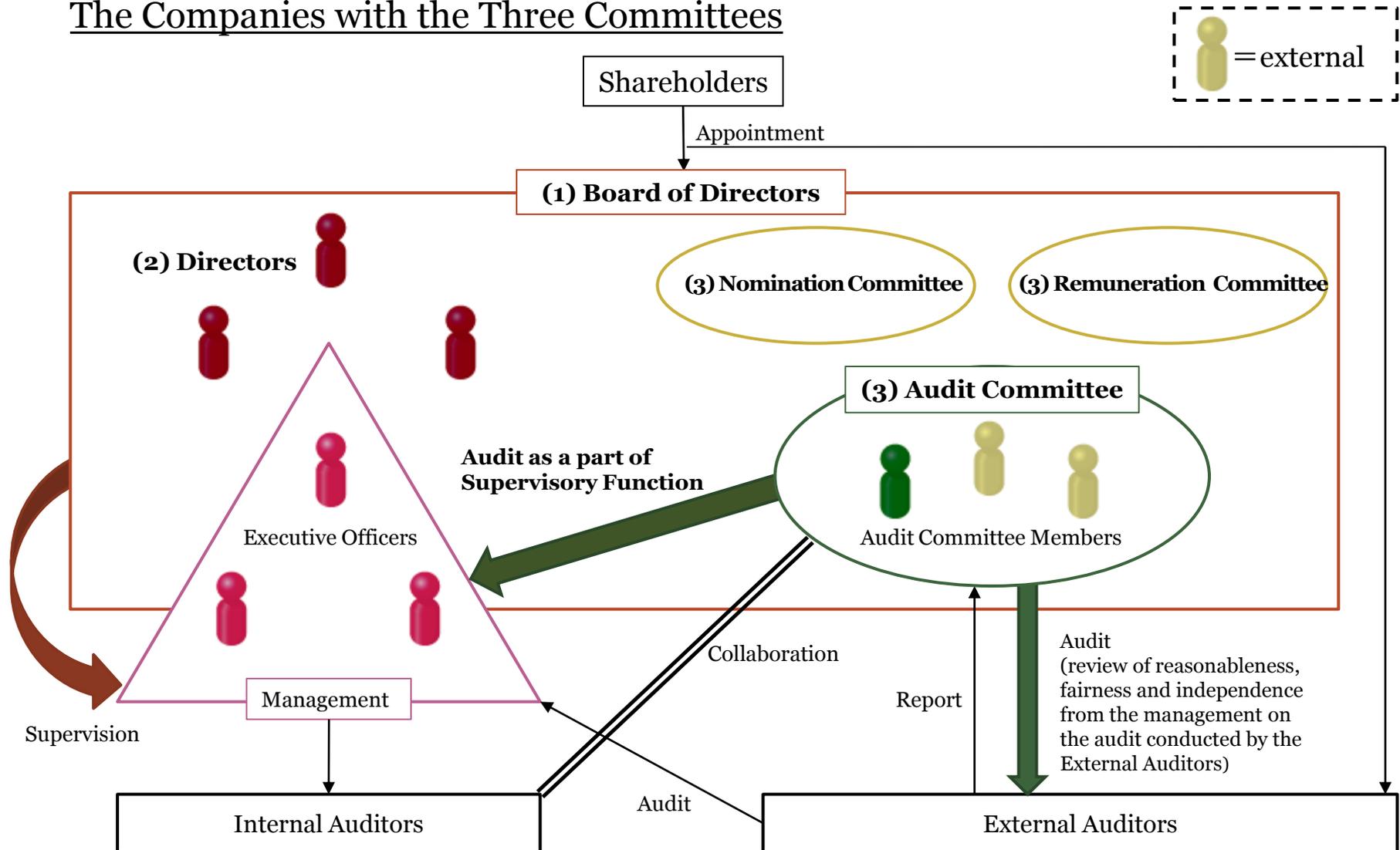
The major supervisory functions of the Members are “checking and monitoring management activities, including abuse of power by management over the external auditors” and “reporting (with opinions) to the Board of Directors”.

(4) Individuality

Except for some prescribed matters, namely (1) preparation of audit reports, (2) appointment and removal of full-time Members and (3) preparation of annual audit policy and coordination of the roles among the Members such as allocation of territories and/or commodities to be audited by each Member and (4) consent to appointment and removal of the External Auditors, which need decisions by the Audit & Supervisory Board (hereinafter referred to as the “A&S Board”), each Member is expected to perform his/her roles individually (not as a body). Although it would not prevent the Members from consulting among them or acting jointly, legal effects of their activities shall be treated as several.

1 Corporate Governance in Japan (two different systems)

The Companies with the Three Committees



1 Corporate Governance in Japan (two different systems)

Features of the Companies with Three Committees

(1) Board of Directors

The Board of Directors basically specializes in supervisory functions. It delegates the management of the company to the executive officers.

(2) Directors

Each Director can act as a member of management as well as a member of the Board of Directors if elected as an Executive Officer by the Board of Directors.

(3) Three Committees

The Three Committees are formed under the authorities of the Board of Directors. Members of each committee are appointed by the Board of Directors from among the Directors. Majority of its members must be external Directors. Functions of each committee are as follows;

- “Nomination Committee”
to propose nomination and dismissal of the Directors at the shareholders meeting.
- “Remuneration Committee”
to determine the remuneration for each Director and Executive Officer.
- “Audit Committee”
to audit activities by management. Its major functions are “checking and monitoring management activities, including abuse of power over the external auditors” and “reporting (with opinions) to the Board of Directors”.

1 Corporate Governance in Japan (two different systems)

Under the Companies Act, private/closed or small or medium sized companies are not required to form the A&S Board though one or more Members are required.

Why the new translation is considered to be appropriate even if no Audit & Supervisory Board is formed

- The term “Audit & Supervisory Board Members” is an English translation of *Kansayaku*, an organ of a Japanese company. Due to its uniqueness, *Kansayaku* is said to be difficult for overseas people to understand. In order to ensure understanding by overseas people on *Kansayaku*, we judged it best to focus on its supervisory functions to be performed in collaboration with the Board of Directors.
- While there exist companies with *Kansayaku* which do not have a board, we do not think it wise to prepare a different translation because *Kansayaku* has only one common definition under the Companies Act. *Kansayaku* exercises its powers and authority individually even if its board is formed. In addition, we should emphasize a virtual board consisting of the Board of Directors and *Kansayaku*, which performs supervisory functions in collaboration with each other even if no board is actually formed. In this sense, we feel it better to use the word “board” even if no board is formed, in order to facilitate understanding by overseas people.

2 Comparison of the Audit & Supervisory Board Members and the Audit Committee

Commonality between the two bodies

Function : Audit and Supervising

Differences between the two bodies

(1) Source of Authority

- The Members
The Members are appointed by the shareholders. The Members are independent of the Board of Directors though they must collaborate with each other in performing supervisory functions.
- Audit Committee
Members are appointed by the Board of Directors from among the Directors. Audit Committee acts under the control of the Board of Directors.

(2) Exercise of Power and Authority

- The Members
Each Member is expected to perform its roles individually (not as a body). Although it would not prevent the Members from consulting among them or acting jointly, their responsibility, legal effects of their activities shall be treated as several.
- Audit Committee
Each member has no individual power and authority. Powers and authority are given to the Committee as a body.

(3) Relationship with administrative sections, such as internal audit division

- The Members
Although the Member(s) and respective administrative sections are expected to collaborate with each other, the Member(s) has no authority to direct these sections because they are under the control of management.
- Audit Committee
Under the authority delegated by the Board of Directors, the committee has the authority to direct them.

3 Comparison of the Audit & Supervisory Board Members and the Audit Committee Members

	Audit & Supervisory Board Members	Audit Committee Members
Appointment	By the shareholders directly	By the Board of Directors
Responsibilities	Audit and Supervision on management activities Preparation of Audit Report to be submitted to the shareholders	Audit and Supervision on management activities Preparation of Audit Report to be submitted to the shareholders
Exercise of Power and Authority	Each member/Individually	Not individual/As committee*
Voting at the Meetings of the Board of Directors	No (though members are required to attend and express their opinion at the meeting)	Yes
Term	4 years	1 year (as director)
Full-time Member	Not required	Not required
External Member	Not required	Majority
Relationship with administrative sections such as internal audit division	No authority to direct (collaboration)	Authority to direct to such extent as delegated by the Board of Directors

* except for preparation of audit report where each Member may express any individual opinion

4 Who are “the Audit & Supervisory Board Members”?

The Members are;

- Appointed by the shareholders.
- Not allowed to be a Director of the company where they are appointed as a Member.

Types of the Members

- Full-time/Standing

The Members who are normally stationed at the principal place of business of the company and spend main part of their working time to perform their duties as Members. They can easily get information on the operation and affairs of the company through constant contact with all relevant company sections.

- External

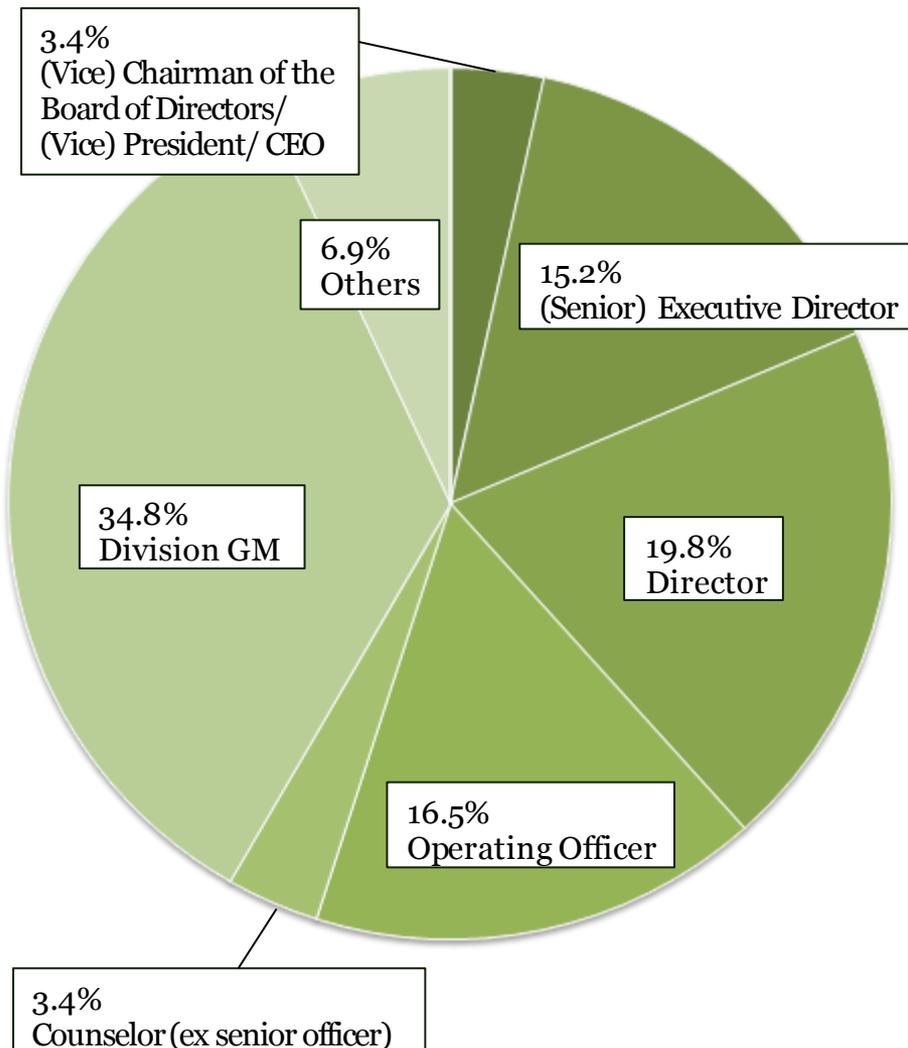
The Members who satisfy the prescribed requirements on independence from the management of the company. Neutral and fair assessment is expected without being affected by the operations and affairs of the company.

➔ Existence of various types of Members enables supervision from different angles.

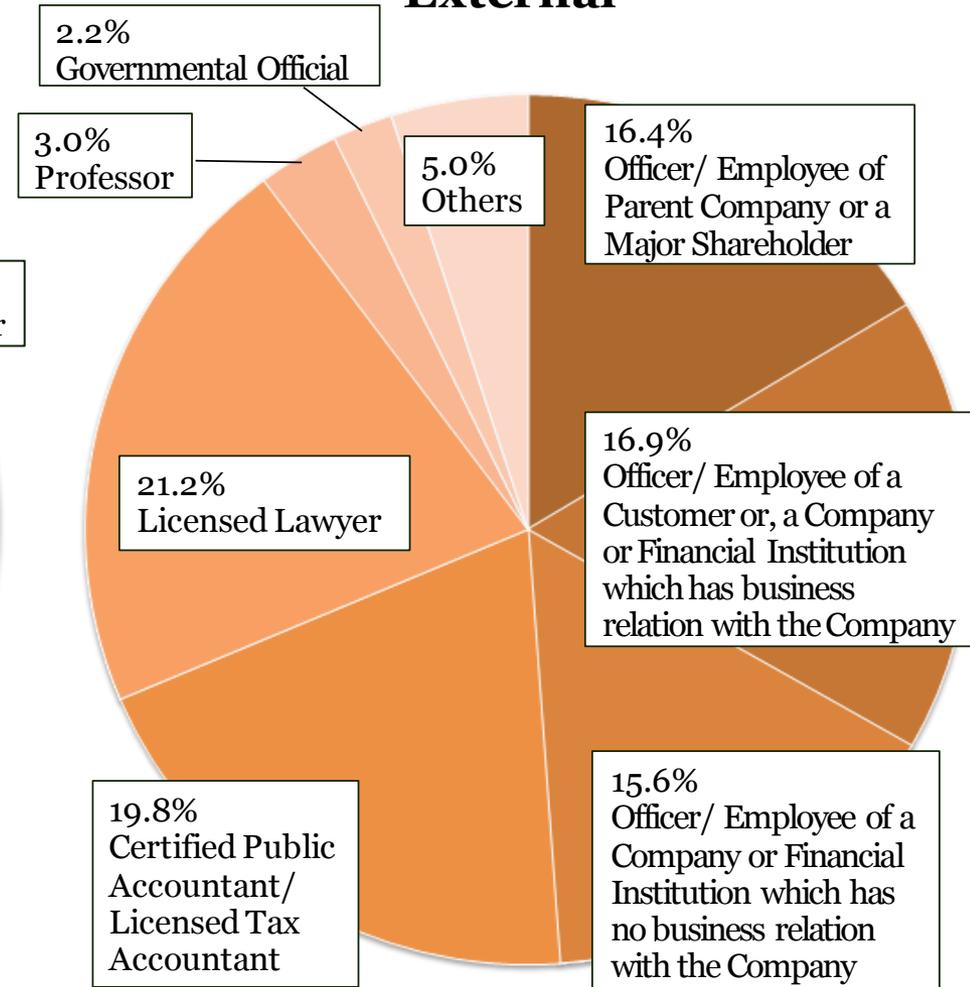
4 Who are “the Audit & Supervisory Board Members”?

Career Background

Company Related



External



Extract from the 13th Internet Survey by JASBA

5 Activities of the Audit & Supervisory Board Members

Among their powers, rights and obligations, the Members have the following as primary:

(1) Research & Investigation

- Power to order officers and employees to report to them operations and affairs of the company.
- Power to investigate operations, financial status and affairs of the company.
- Power to investigate operations, financial status and affairs of subsidiaries.

(2) Actions on operation of the company

- Obligation to attend and express their opinions at the meeting of the Board of Directors.
- Power to convene a meeting of the Board of Directors.
- Right to seek an injunction against an act by the Directors if certain requirements are satisfied.

(3) Actions on external auditors

- Power to order the external auditors to submit final/interim report on their audit.
- Right to consent to the Directors on submission to the shareholders meeting of their proposal on appointment or removal of the external auditors.
- Right to consent to the Directors on fee for the external auditors.

(4) Reporting

- Obligation to submit their audit report and perform supplemental explanation at the annual shareholders meeting.
- Obligation to investigate and report the result to the shareholders meeting if any violation of laws and regulations or constituent documents, or any material injustice is found in a proposal or its related materials to be submitted to the shareholders meeting.

(5) Legal action against Directors

- Obligation to examine and judge the reasonableness of a request by a shareholder to take legal action against a Director or Directors for his/her (their) breach of duty of care and/or fiduciary duty to the company and if such request is considered reasonable, to take legal action against them as a representative of the company.

5 Activities of the Audit & Supervisory Board Members

The Members conduct various activities to fulfill their duties and responsibilities.

(2) Communications
with the external auditors

(3) Communications
with the internal auditors
and their staff

(1) Hearing
from directors, officers and
employees

Meeting of the Members

- Preparation of Audit Report
- Preparation of Audit Plan
- Examination of materials to be submitted to the meetings of the Board of Directors
- Report from full time/standing Members on their activities
- Hearing from the external auditors on their audit report

(4) On-site survey
at offices/factories etc of the
company and its subsidiaries
and affiliates (including
overseas)

(5) Communications
with the Members/Audit
Committee Members of
subsidiaries and affiliates

(6) Inspection
of constituent documents and
other important documents

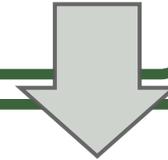
(7) Attending and
expressing opinions
at the meeting of the Board
of Directors

5 Activities of the Audit & Supervisory Board Members

Typical Annual Action Plan of the Members is as follows;

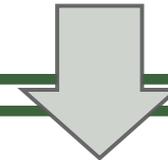
Immediately after Annual Shareholders Meeting (Normally within 3 months after the end of each financial year of the company)

- Preparation of annual audit plan
- Coordination of schedule with the sections concerned (including the external auditors)



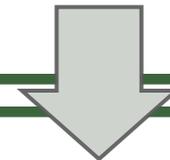
During each financial year of the company

- Hearing from the management of the company
- On-site survey
- Inspection of constituent documents and other important documents



End of each financial year of the company

- Preparation of Audit Report
- Examination of accounting documents and business report prepared by the management of the company



At the Annual Shareholders Meeting after the end of each financial year of the company

- Report to the shareholders the result of the audit in writing which could be supplemented verbally
- Q&A Session

6 Roles of the Audit & Supervisory Board Members for prevention and settlement of misconduct and wrongdoing

The Members shall contribute to prevention of occurrence of misconduct and wrongdoing through their ordinary audit and supervisory activities and shall timely take appropriate actions in order to minimize damage to the company.

