

# OASIS

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Submission by:

Oasis Management Company Ltd.  
21/F Man Yee Building  
68 Des Voeux Road Central  
Central, Hong Kong  
[Email: sfischer@hk.oasiscm.com](mailto:sfischer@hk.oasiscm.com)  
Tel: +852 2868 3722

To the Advisory Group to Review TSE Cash Equity Market Structure:

We wish to commend the TSE for its efforts to seek feedback on how to further improve the integrated market structure of the TSE and OSE markets. As a long-time participant in the Japan capital markets, we here respectfully submit our comments to the December 21, 2018 “Review of the TSE Cash Equity Market Structure” consultation paper.

Please see Oasis’s suggestions for TSE market structure below. We submit these suggestions in the interest of developing a sustainable, investable index in Japan for all global investors, which will reduce the cost of capital for listed companies by raising valuations, provide long-term attractive investment options for investors, and positively affect Japan’s economy.

You will note that our comments do not strictly track the consultation paper’s numbering. Instead, we have presented our ideas for a fresh set of index structure improvements and innovations that we would like to see.

## **1. Creation of a new “TSE450” (which would enable a TSE Premier Index)**

The TSE450 Section and Index would comprise the largest 450 stocks by market capitalization listed today in TSE1, TSE2, JASDAQ and Mothers indices, as long as they meet the following criteria:

- a) Trailing 18-month average market capitalization of over 50 billion yen;
- b) Trailing 6-month average market capitalization greater than the average 6-month market capitalization of the 451 largest stocks by market capitalization in the current index; and,
- c) All changes to be announced semi-annually, with a measuring period to be ended 30 days prior to the rebalance date.

And fulfill the following Corporate Governance criteria:

- i. Unwind cross-shareholdings<sup>1</sup> (over an 18-month period);
- ii. Use an electronic voting platform;
- iii. Eliminate vote by clapping at AGMs;
- iv. Grant access to company senior management for shareholders owning more than a 3% stake on a semi-annual basis;
- v. Have an appointed lead independent director (“筆頭独立社外取締役”);
- vi. Have a majority of independent board directors;
- vii. All directors are responsible for: oversight of executives, maximizing long-term shareholder value, and assessing business strategy, performance and corporate governance;
- viii. Have independent nomination, compensation, and audit committees comprised of independent directors of the board;
- ix. Require majority of minority shareholder approval for all transactions of over 10% of the company’s net asset value (e.g., tender offers, share exchanges, mergers, etc.);
- x. Implement board diversity gradually (targeting a minimum of 5% women by 2020, 10% women in 2021, 15% in 2022, and minimum of industry expert independent directors, targeting 5% by 2020, 10% in 2021 and 15% in 2022);
- xi. Have their corporate pension funds sign the Stewardship Code;
- xii. Disqualify board members from serving as a board member of a public company for 3 years following submission of false accounts or qualified accounts;
- xiii. Implement share-based compensation at a minimum 10% of total compensation;
- xiv. Hold strategy discussions at board meetings;
- xv. Publicly disclose the length of board meetings;
- xvi. Provide quarterly disclosure;
- xvii. Provide equal English & Japanese disclosure;
- xviii. Allow investors (and holders of shares including shares held in street name in Brokerage accounts) to appoint an AGM/EGM representative, enabling the underlying shareholder (e.g., CIO, PM or analyst) to attend and vote the fund’s shares at the AGM/EGM;
- xix. Hold Treasury stock of no more than 5% based on an annual test;
- xx. Disclose all Komons (“顧問”) and Sodanyaku (“相談役”) and all benefits paid to them;

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<sup>1</sup> Cross-shareholdings defined here as shareholdings in another listed Japanese company with which the company has a business relationship that have been held for more than 5 years. (I.e., companies can hold shareholders in listed subsidiaries or other companies for a period of up to 5 years.)

- xxi. Have stated targets for cost of capital, ROIC, ROE, and provide explanations for any failure to meet targets (to be included in the Yuho (“有価証券報告書”));
- xxii. Eliminate poison pills (“買収防衛策”);
- xxiii. Conduct split voting (“累積投票制度”) (i.e., shareholders get one vote per share held, multiplied by the number of directors to be elected), allowing minority shareholders to elect a representative to the board;
- xxiv. Separate duties between Chairman & CEO;
- xxv. Have an independent chairman;
- xxvi. No squeeze-out of minority shareholders if the majority shareholder owns less than 90% (as per Article 179 of Japan’s Companies Act) (“株式等売渡請求権”によるスクイズアウト) (i.e., elimination of the application of Articles 235 enabling the “share consolidation” method of squeeze outs of minorities) (“全部取得条項付種類株式”によるスクイズアウト); and,
- xxvii. Maintain a minimum of 25% free float.

Delisting (for a period of 2 years from the time the breach is rectified) should occur on a quarterly basis, with no than 4 months granted to “cure” any breach Delisting should be strictly enforced for any company that:

- i. Submits fraudulent accounts;
- ii. Has any “going concern uncertainty” in its auditor reports;
- iii. Does not submit audited accounts;
- iv. Submits qualified accounts;
- v. Has 5 years of negative equity;
- vi. Has 5 years of ROE under 3%, if the most recent year is not above 3%; and,
- vii. Conducts any activity that results in a regulatory fine and went on for 5 years or more (after a two-year grace period).

Demotions and changes from the index:

A TSE450 company can be demoted from the TSE450 index if its market capitalization falls below the market cap of the top 500 companies (combining the TSE450 and the TSE Regular index) for a period of 18 months. A stock from the Regular TSE that fits the TSE450 criteria should replace it.

## **2. Creation of the TSE regular index**

With the following criteria:

- i. Provide semiannual disclosure;
- ii. Provide simultaneous Japanese and English disclosure;
- iii. Maintain a minimum of three independent directors;
- iv. Grant access to company senior management for shareholders owning more than a 5% stake;

- v. Disclose all Komons (“顧問”) and Sodanyaku (“相談役”) and all benefits paid to them;
- vi. Hold Treasury stock of no more than 5% based on an annual test; shares in excess of 5% must be cancelled;
- vii. Have a lead independent director (“筆頭独立社外取締役”);
- viii. Require majority of minority shareholder approval for all transactions over 10% of the company’s net asset value (e.g., tender offers, share exchanges, mergers, etc.)
- ix. Conduct split voting (“累積投票制度”) (i.e., shareholders get one vote per share held, multiplied by the number of directors to be elected), allowing minority shareholders to elect a representative to the board; and,
- x. Maintain a minimum of 25% free float.
- xi. Minimum market capitalization of over 5 billion yen.

Delisting (for a period of 2 years from the time the breach is rectified) should occur on a quarterly basis, with no than 4 months granted to “cure” any breach. Delisting should be strictly enforced for any company that:

- i. Submits fraudulent accounts;
- ii. Has any “going concern uncertainty” in its auditor reports;
- iii. Does not submit audited accounts;
- iv. Has 5 years of negative equity;
- v. Has 5 years of ROE under 3%, if the most recent year is not above 3%; and,
- vi. Conducts any activity that results in a regulatory fine and went on for 5 years or more (after a two-year grace period).

### **3. Creation of the Emerging Growth Section (similar to Mother’s Section today)**

With the following criteria:

- i. Less than 10 years of operating history in the company’s current business;
- ii. Companies must not remain on the index for more than 7 years; and,
- iii. Require majority of minority shareholder approval for all transactions.

### **4. Creation of a Pink Sheet Section**

Creation of a Pink Sheet section for all companies that do not fit into any of the above categories. The Pink Sheet section will be the listing vehicle for any companies not in compliance with, or demoted from, the TSE Premier 450, The TSE Regular listing, or the Emerging Growth Section.

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We are available to discuss and elaborate on these suggestions at any time. Thank you.

Respectfully submitted,

Seth H. Fischer  
Founder & Chief Investment Officer  
Oasis Management Company Ltd.