

DIALOG

Corporate Governance System for Creating a 100-Year Company

In September 2022 taking advantage of the Group reorganization, the Avant Group became a company with an Audit and Supervisory Committee.

Ms. Goto, an Independent Outside Director (Audit and Supervisory Committee Member), and Mr. Noshiro, a Director (Audit and Supervisory Committee Member) discussed the purpose of the transition and the ideal group structure.

Objective of Transition to a Company with an Audit and Supervisory Committee

Goto I was appointed as an Outside auditor of Avant Corporation (currently Avant Group) in September 2021. Had you been considering a transition to a company with an Audit and Supervisory Committee before that?

Noshiro After the number of outside directors became a majority in September 2020, there have been notably more opinions that the board of directors should spend more time discussing strategy than detailed business execution. To this end, my understanding is that a company with an Audit and Supervisory Committee structure is better able to delegate authority for business execution and is therefore desirable.

Goto My understanding is that our Company has shifted to a company with an Audit and Supervisory Committee because we have tended to have a monitoring type of Board of Directors rather than a management type. As you said, if there are many outside

directors, I think it would be desirable for the Board of Directors to utilize the knowledge of outside persons in decision-making on important business execution and supervision of execution, rather than making decisions on a wide range of business execution matters. Certainly, at the time of the transition to a company with an Audit and Supervisory Committee, the number of Outside Directors including Audit & Supervisory Committee Members decreased by one from the previous five to four. However, in terms of the number of Directors, four out of seven Directors (including Audit and Supervisory Committee Members) are Outside Directors, which is no different from the previous line-up in which three out of five Directors were Outside Directors.

Noshiro We believe that the more the independent outside directors (including audit and supervisory committee members) vote, the more we make decisions based on diverse values and that this contributes to the creation of a 100-year company. On the other hand, at first glance it can be said that

with diversity and inclusion, it could become easier to generate votes against proposals, but I think the answer to this is to operate the meetings so that ever more thorough discussions are possible. Based on the comments made at the Board of Directors meetings since her appointment, there have been opinions that we should make more effective use of Ms. Goto's value as a director.

Goto Some people may have the impression that the change from Auditors to Directors (Audit and Supervisory Committee) for Mr. Noshiro and I is cosmetic. However, in reality, we have the right to vote in the selection of representative directors and on decision-making on the execution of extremely important business operations, as well as the authority to state opinions at the General Meeting of Shareholders regarding the appointment, dismissal and remuneration of directors who are Audit and Supervisory Committee Members, and as such I feel that we are in a position of much greater responsibility than corporate auditors. From now on,



CHIE GOTO

Director (Audit Committee Member)
Outside, Independent Director

TSUYOSHI NOSHIRO

Director (Audit Committee Member)

Mr. Noshiro, who works full-time and has a deep understanding of the Company, Mr. Nakano, who is an expert on corporate value, and I, who is an expert on legal matters, we hope to make an Audit and Supervisory Committee that can effectively exercise supervision over the execution of business. Except for matters reserved by law, I hope that the Board of Directors will be able to, in a timely manner, flexibly create the optimal balance between execution and supervision, and take advantage of the most important advantage of a company with an Audit and Supervisory Committee, which is the ability to delegate decision-making related to the execution of important business operations to directors.

Noshiro In my opinion, it would be better for the Board of Directors not to make a hasty decision on the transfer of decision-making authority to executive directors. This is because I believe that it would be in line with our management philosophy of "Creating a 100-Year Company" to review the transfer of authority when we have changes in the composition of the board, or the Group CEO changes in the future. I think it is a good thing that in the recent revision of the Board of Directors Regulations, the items of authority to be transferred are confirmed every year after the General Meeting of Shareholders.

Aim of Changing the Organizational Design at the Same Time as the Group Reorganization

Goto There are some views that given the importance of the Company's reorganization, it may have been better that the Company shifted to a

company with an Audit and Supervisory Committee at a later date. What do you think of this opinion?

Noshiro My understanding is that this change in organizational design is linked to the change in the group's management system following the reorganization. Under the new structure, Group CEO Morikawa mainly formulates strategies, while Group COO Okabe and Group COO Nagata lead and execute the organization based on these strategies. My view is that "organizations follow the strategy."

I think a company with an Audit and Supervisory Committee, where the board is more of a monitoring function is more appropriate because it separates strategies from execution (organizational composition) and creates an environment in which Mr. Morikawa can concentrate on group strategies and fewer items regarding execution will make it to the board agenda.

Goto As a background to the reorganization of the Company, it has been pointed out that insufficient communication with the team executing the Company's management strategy was one of the reasons why the transformation to the business model targeted in "BE GLOBAL 2023" did not proceed well. With the separation of strategic decision making by top management from its execution, there is a need to clearly define how the two sides interact, which also requires strengthened communication, and as such I think that to achieve this it was necessary to make the transition to a company with an Audit and Supervisory Committee at the same time.

Noshiro The adoption of the Group Corporate Officer System and the establishment of CxO positions is part of the separation of the Group's strategy and execution.

In addition, to make the Audit and Supervisory Committee Rules more monitoring oriented, we have changed the part of the model of the Japan Audit & Supervisory Board Members Association in which authority is somewhat concentrated on internal Audit and Supervisory Committee Members so that outside Audit and Supervisory Committee Members can play an active role. For example, in the model, Audit and Supervisory Committee Members who have the right to investigate business assets and subsidiaries are selected, and these selected Audit and Supervisory Committee Members can do anything, but the Audit and Supervisory Committee Members who are not selected cannot do anything. For this reason, we have proposed a rule to separate the items that should be investigated by an internal Audit and Supervisory Committee Member and the items that should be investigated by an external Audit and Supervisory Committee Member, and to select a member in charge of investigation for each of them.

Goto As a lawyer, I have the opportunity to check similar regulations of other companies, but I have the impression that companies are generally not proactive about deviating from the model. There will be a problem if there is a discrepancy with the legal regulations, and I think it can simply be troublesome to forge your own path while maintaining consistency. But in this case, I feel that the Company's efforts to make changes to various provisions with intent of creating an ideal system for the Audit and Supervisory Committee, is an indication of the Company's desire for ideal governance.

Noshiro Additionally, I personally felt that this reorganization of the Group



I think that a wide range of diversity beyond just skills is important.

CHIE GOTO

was a particularly big decision, as not only did Mr. Morikawa step down as President of the former Diva, which he founded as the origin of the Group, but we also split the former Diva into two companies, making this decision to step down irreversible. With the impossibility of Mr. Morikawa being able to return as head of the former Diva, the further separation of execution means that we are also making a little progress with the potential succession of the Group CEO.

Goto Mr. Noshiro you are capable of such insightful analysis because you have followed our company's progress for a long time.

Ideal Corporate Governance System

Noshiro In designing an organization, a company with a Nominating and Supervisory Committee, etc. may be an option, but if it is only presentation of proposals, I am against it. The reason for this is that under the current Japanese Companies Act, the composition of the Board of Directors is determined solely by the members of the Nominating Committee, and outside directors who are not members of the Nominating Committee do not have any right to vote on the composition of the Board of Directors. Thus, if there are seven directors and a majority are outside directors, as was the case of the Company, governance will be weakened.

Goto The Company has established a voluntary Compensation Advisory Committee, and I am one of the committee members. The Committee proposes specific compensation for Directors and Executive Officers, and although it is an optional advisory committee, I believe that it fulfills a certain supervisory function. The Audit and Supervisory Committee has the authority to express its opinions on the remuneration of Directors who are Audit and Supervisory Committee Members. In addition, linking this to the fact that the Compensation Advisory Committee is functioning in a specific manner, the Company has established a system in which it is easy to exercise its management evaluation function in terms of remuneration and personnel affairs. As a member of the Compensation Advisory Committee,

Strengthening the link between the compensation system for directors and the next medium-term management plan is a key to strengthening the oversight under the new structure.

TSUYOSHI NOSHIRO



I feel the weight of my responsibility, but I feel that exercising this evaluation authority will fulfill my role.

Noshiro I feel that governance is really getting stronger gradually since the Compensation Advisory Committee was established. Strengthening the link between the compensation system for directors and the medium-term management plan to be launched in July 2023 is a key to strengthening the oversight of the executives under the new structure.

Goto Looking forward, I think the challenge is board configuration and succession. What about you, Mr. Noshiro?

Noshiro I agree. This is a personal idea that I have never referred to at the Board of Directors' meeting, and if I propose it, there may be opinions against it, so, we need to discuss it

carefully. However, regarding the succession of outside directors, I think that one candidate should be proposed by the Group CEO and another candidate should be selected by a meeting of outside directors. In other words, if there is diversity in the mother body who chooses the candidate, the diversity will progress.

Goto I see. It's interesting idea that a wide range of people can become candidates rather than just choosing candidates by the same person or by the same route.

Noshiro It is based on the idea that it is not necessarily good for the Group CEO to be continuously involved in all the appointments if we truly aim to "create a 100-year company." The fact that it was just the Board of Corporate Auditors that selected you, Ms. Goto as

a candidate in 2021 may have given me about the inspiration for this idea.

Goto In the future, when considering the composition of the Board, reflecting management strategy at the time, I think it will be necessary to further refine the skill matrix and to consider the diversity of attributes such as gender, nationality, and generation. If you just choose people who fit the skills you want now, you won't be able to come up with new ideas. From a long-term perspective, I think that a wide range of diversity beyond just skills is important.

Noshiro There is probably no right answer as to what kind of board structure is good, it is something we need to hear various opinions on and continue discussing.