



Principles of Corporate Governance for Listed Companies

Tokyo Stock Exchange, Inc.

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Tokyo Stock Exchange, Inc.



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Principles of Corporate Governance for Listed Companies



Preface

All around the world more attention than ever before has been directed at the importance of corporate governance.

In every country, corporate scandals and long periods of depressed performance results have focused companies' attention on the importance of corporate governance. - As such, corporate governance has now been steadily and widely adopted on a global basis with a growing recognition that it is certain to have an impact on corporate competition as corporations adapt to rapid economic globalization.

More and more voices have been raised in demand for enhanced corporate governance in the every country's securities markets. Though stock exchanges, the operators of securities markets, have been fulfilling their important duty of enhancing corporate governance in major securities markets worldwide, the approaches undertaken by individual stock exchanges to enhance corporate governance have not converged.

In light of countries' differing legislations and legal bases for corporate governance, the issue cannot easily be compared across different countries. Fortunately, however, there have been positive developments. For example, New York Stock Exchange formulated a set of minimum standards on corporate governance in its Listing Standards, with which listed companies must comply. In Europe, the London Stock Exchange stipulates a best practice code for corporate governance whereby any company that adopts policy divergent from this code must explain why.

These Principles of Corporate Governance have not been designed to stipulate a specific model policies or aggregations of policies on corporate governance as the best or minimum standards for corporate governance. Therefore, the purpose of these Principles is not to require listed companies to adopt minimum standard policies or models for corporate governance, nor to demand companies that do not adopt the best policies or models to explain why.

The purpose of these Principles is to provide a necessary common base for recognition, thereby enhancing corporate governance through the integration of voluntary activities by listed companies and demands by shareholders and investors.

Why are these Principles determined for the purposes described above? By taking into account the present condition of and environment surrounding companies listed on Tokyo Stock Exchange, we believe that approaches such as those mentioned above will be highly effective in enhancing their corporate governance.

Some people argue that amidst the financial structure centering on indirect financing and cross shareholding, shareholders have traditionally had only a minor influence on companies and

have not been strongly motivated to monitor management to their own benefit, and thus their interest in corporate governance has also been weak. Recently, however, listed companies have been implementing voluntary measures needed to enhance corporate governance in response to the development of the globalized economy and elimination of cross shareholdings. Furthermore, these initiatives have been fuelled further as foreign and domestic institutional investors express their opinions and demand their rights more strongly than before.

There has been a trend in many companies to adopt measures of strengthening the responsibilities of outside auditors, introducing an executive officer system and electing external directors, but the measures adopted at individual companies vary considerably.

In this context, the Commercial Code was amended to strengthen the corporate auditor system. Pursuant to the amended Commercial Code that took effect in April 2003, listed companies have been granted options for the introduction of a committee system as well as an auditor system, and the effective use of these options has been seen to further enhance governance.

In the circumstances where various measures for enhanced corporate governance have been sought, and the legal framework enabling these various options has improved, it is essential the effort of listed companies should lead to enhanced corporate governance. To this end, listed companies should compete each other for achieving more enhanced corporate governance through the evaluation by investors. That is the basic concept for these Principles.

In this respect, the concept for these Principles is at a level consistent with the OECD Principles of Corporate Governance and the main components of the report prepared by the private advisory committee to the OECD. The respective items in these Principles have been set forth pursuant to the structure of the OECD Principles.

Principles of Corporate Governance for Listed Companies

Corporate governance is generally defined as the framework for disciplining corporate activities.

Most corporate activities have been undertaken principally with a view to generating revenue and thereby enhance the corporate value to shareholders. In expecting the listed companies to generate such performance on a continuous basis, it inevitably becomes necessary to motivate or monitor the management accordingly through a framework for disciplining corporate activities, namely corporate governance.

In other words, the appropriate operation of corporate governance for listed companies is a vitally fundamental demand for enhancing corporate value on a continuous basis, and the underlying aims of corporate governance are to provide an environment for such enhancement.

The profit-pursuing activities of enterprises are not fulfilled in modern economic society without complicated coordination of interests among various concerned parties (shareholders or investors, management, employees, suppliers, creditors, and local communities). As the areas of corporate activity are expanding, corporations face a growing need to take into account the values of different cultures and societies. As such, enterprises will have to engage in their profit-pursuing activities with a greater awareness of their social responsibilities, with greater transparency and fairness in accordance with market principles, while accepting full accountability to the entire economic community as well as shareholders and investors. The relationship with every concerned party bears an influence on corporate governance. From the perspective of the capital market, its focus centers primarily on relations between shareholders (including potential shareholders) and management.

The authority to execute the business of the company is delegated in large part to the management (representative directors, executive officers and directors, principal executives and the like), however such authority is based upon the confidence of shareholders, who ultimately provide the capital and bear the risks.

Shareholders usually empower the directors and auditors they elect with the authority to appoint, supervise and motivate management for the purpose of maximizing corporate value. Management is appointed by the resolution of the board of directors, which is given the authority to execute daily routine work, and permitted to exercise broad authority subject to the supervision of the board of directors and board of corporate auditors. Directors, auditors, and the board of corporate auditors are elected by shareholders and have the obligation as prudent managers to fulfill the responsibilities mentioned above and the perform duties faithfully for the company and

shareholders.

Any of the above can serve as a framework for governing the relations between shareholders and management. How to operate them effectively is the core issue of corporate governance.

Corporate governance, i.e., the framework for disciplining corporate activities, particularly those pertaining to the relationship between shareholders and management, is expected to fulfill various functions. The most important of these functions are as follows. Above all, it is crucial that the rights and interests of shareholders be protected and equally secured. Secondly, respecting the basic rights and interests of concerned parties other than shareholders (whose responsibilities have been increasing), and building smooth relationships with other such parties are crucial to the enhancement of a company's corporate value. In taking steps to effectively protect the rights and interests of all these interested parties, the transparency of corporate activities must be secured through the timely and accurate disclosure of information. Finally, the board of directors, auditors, and board of corporate auditors all hold key responsibilities and must fulfill all the duties expected of them.

These functions expected of corporate governance should be realized through the actual corporate governance policies adopted by a company. In reality, however, a specific model with a set of policies alleged to enhance corporate governance may not apply to every enterprise, but there are various combinations of policies suitable for individual enterprises. More important than adopting actual policies for corporate governance is the duty of individual companies to search for methods to better fulfill these functions in the light of cost-benefit relations to achieve the desired results.

The basic principles of a market economy hold that shareholders and investors evaluate these efforts and the state of information disclosure to make investment judgments and exercise their voting rights. Individual companies should review and improve their efforts on the basis of such evaluation.

The following points, as Principles of Corporate Governance, raise the issues to which all companies should direct their attention, based on the expected functions of corporate governance.

1 Rights of shareholders

Corporate governance for listed companies should protect the rights of shareholders.

Corporate governance has been structured with the primary focus on shareholders. There are many stakeholders (concerned parties) other than shareholders who have relationships with companies. They include employees, creditors, suppliers, customers, and communities. Indeed, the continuous profit from corporate activities would not be generated without smooth relationships with these stakeholders. However, looking at corporate governance from the perspective of a capital market, the shareholders (i.e. the providers of the capital) lie at the core of corporate governance.

For the purpose of fulfilling their responsibilities as the element at the core of corporate governance, shareholders shall be authorized to exercise various rights in managing a company. This should include the right to participate and vote in general meetings of shareholders on basic decisions of the company, including elections and dismissals of directors and auditors, fundamental corporate changes, the basic right to share various profits such as dividends, and the special right to make derivative lawsuits and injunction of activities in contravention of laws, regulations and other rules. That these rights as established by law should be protected and secured is the underlying condition for the proper function of corporate governance in conjunction with shareholders' awareness of their rights.

Issues requiring attention

Listed companies shall direct their attention to the following issues in order to protect the rights of shareholders:

- (1) Respect of shareholders' basic rights
 - a. Respect of voting rights
 - i . Development and improvement of an environment in which shareholders exercise voting rights appropriately;
 - ii . Development and improvement of an environment in which shareholders are inclined to participate in general meetings of shareholders;

iii. Mutual communication with shareholders at the general meetings of shareholders;

b. Return of profit to shareholders

(2) Due consideration to the infringement of rights of existing shareholders

a. Enhanced disclosure of information to shareholders in situations where specified shareholders have excessive control that is not in proportion to the ownership ratio, and the rights of other shareholders are substantially infringed.

b. Securing fair treatment of and enhanced information disclosure to shareholders in cases where the ownership distribution of the company is, or will be, changed.

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Equitable treatment of shareholders

Corporate governance for listed companies should ensure the equitable treatment of all shareholders, including minority and foreign shareholders.

The equitable treatment of all shareholders of the same class in proportion to their equity interests is an important element of corporate governance. Management, directors, auditors and controlling shareholders may find opportunities to abuse their positions to benefit themselves, and such activities are certain to cause disadvantages to investors and minority shareholders. The prohibition of abusive or fraudulent use of corporate assets or insider information by parties closely related to the company is an inevitable step to be taken both to protect investors and to maintain their confidence in the capital markets.

Issues requiring attention

Listed companies shall direct their attention to the following issues in order to secure equitable treatment of shareholders:

- (1) Development and improvement of a system to prohibit transactions against the primary interests of the company or shareholders through the abuse of concerned parties' positions such as officers, employees, and controlling shareholders;
- (2) Enhanced disclosure of information to shareholders in cases where concerned parties conduct actions that are likely to damage the primary interests of the company or shareholders;
- (3) Prohibition of special benefits provided to specified shareholders.

3

Relationship with stakeholders in corporate governance

Corporate governance for listed companies should help create corporate value and jobs through the establishment of smooth relationships between the company and its stakeholders and encourage further sound management of the enterprise.

That companies sustain and improve their competitive strengths and enhance their values through the pursuit of profit on a continuous basis is a principal interest common to shareholders, but this is the result of the provision of company resources by all stakeholders. Thus, the establishment of smooth relationships with stakeholders other than shareholders based on active cooperation and constructive criticism would be in the long-term interests of enterprises.

Issues requiring attention

Listed companies should direct their attention to the following issues in order to establish smooth relationships with stakeholders other than shareholders:

- (1) Cultivation of a corporate culture that respects the positions of stakeholders, and development of internal systems therefore;
- (2) Timely and accurate disclosure to stakeholders of material information relating to stakeholders, and development of internal systems therefore.

4 Disclosure and transparency

Corporate governance for listed companies should ensure that timely and accurate disclosure is conducted on all material matters including the financial condition, performance results and ownership distribution.

Listed companies shall be obliged to conduct timely and accurate disclosure regarding corporate activities. Such disclosure is indispensable for appropriate investor evaluation of enterprises in the market, and concurrently for the appropriate exercising of voting rights by shareholders. For this purpose, shareholders require periodic, reliable and comparable information sufficient to evaluate the operational conditions of businesses by the management, and further timely disclosure regarding material events taking place during the intervals between periodic disclosures. Such disclosure shall be conducted simultaneously to ensure equal treatment of shareholders. Fair disclosure helps to secure the confidence of investors in the market and is an important means to prevent the abuse of insider information.

Issues requiring attention

Listed companies should direct their attention to the following issues in order to conduct timely and accurate disclosure:

- (1) Enhanced disclosure of quantitative information on financial conditions and operating results and enhanced disclosure of qualitative information that deepens the understanding of the management conditions of companies by investors ;
- (2) Securing opportunities for investors to access information equally and easily;
- (3) Development and improvement of internal systems to secure the accuracy and promptness of disclosure.

5

Responsibilities of Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s)

Corporate governance for listed companies should enhance the supervision of management by the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s)^(*1), and ensure their accountability to shareholders.

(*1) The term "Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s)" refers to the organization responsible for supervising management, mainly the Board of Directors and Auditors or Board of Corporate Auditors.

The legal framework or basis for corporate governance permits the choice of a corporate auditors system or committees system. In either case, the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s) should evaluate whether the management^(*2) has been accurately and efficiently executing business pursuant to their strategic guidance on strategies, and prevent the occurrence of conflicts of interest between the company and the management by reflecting on such evaluation prior to the election or discharge of management or the execution of decisions on compensation, and thereby fulfill their appropriate supervision responsibilities.

(*2) The term "management" means the persons recognized by the company to have actually been involved in the management of the company, including representative directors and executive officers, which in turn include representative executives and executives.

Issues requiring attention

Listed companies should direct their attention to the following issues to ensure that the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s) sufficiently fulfill their responsibilities for management supervision and accountability to shareholders:

- (1) Monitoring of the management by the Board of Directors and Auditors or Board of Corporate Auditors and other relevant group(s)
 - a. Organization of a Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s) suitable for making an objective determination on the execution of business by the management;

- b. Development and improvement of a system under which the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s) assume responsibility for supervising the management;
 - c. Development and improvement of an internal check and balance system under which the Board of Directors, Auditors, Board of Corporate Auditors, and other relevant group(s) make reasonable judgments on their compliance with laws and regulations and accuracy of business operation conditions.
- (2) Motivation for the management to maximize corporate value through positive convergence of management and company interests by appropriate means.
- (3) Development and improvement of a mutual monitoring system by directors under which fulfillment of duty and integrity as prudent managers should be secured and under which illegal activities and inappropriate activities from the perspective of generally accepted views are prevented.



(Appendix) Mechanism for Corporate Governance in Japan

In Japan, the legal framework prescribes two types of mechanisms for corporate governance that apply to most listed companies: a corporate auditors system consisting of general meetings of shareholders, the board of directors, representative directors, executive directors, corporate auditors, and the board of corporate auditors ("company with a corporate auditors system"); and a committees system^(*) consisting of general meetings of shareholders, the board of directors, and committees composed of members of the board of directors (nomination committee, audit committee, and compensation committee), representative executive officers and executive officers ("company with a committees system"). The selection is left to individual companies.

In either mechanism, general meetings of shareholders, comprised of shareholders who are owners of the company, are the supreme body and decision-making body on fundamental issues of the company. The board of directors is made up of directors elected at the general meetings of shareholders, it is also the decision making body responsible for deciding business execution, and the body responsible for supervising the performance of directors' duties (in the case of companies with a committees system, representative executive officers and executive officers are included).

With respect to a company with a corporate auditor system, representative directors and executive directors serve as the business execution body. Representative directors are elected from among directors by the board of directors. Representative directors represent the company while executive directors are directors other than representative directors who have been nominated to directorships in order to execute business by resolutions of the board of directors and have accepted such nomination. Corporate auditors^(**) are elected at general meetings of shareholders separately from directors and the board of corporate auditors consists exclusively of corporate auditors and audits the performance of directors' duties.

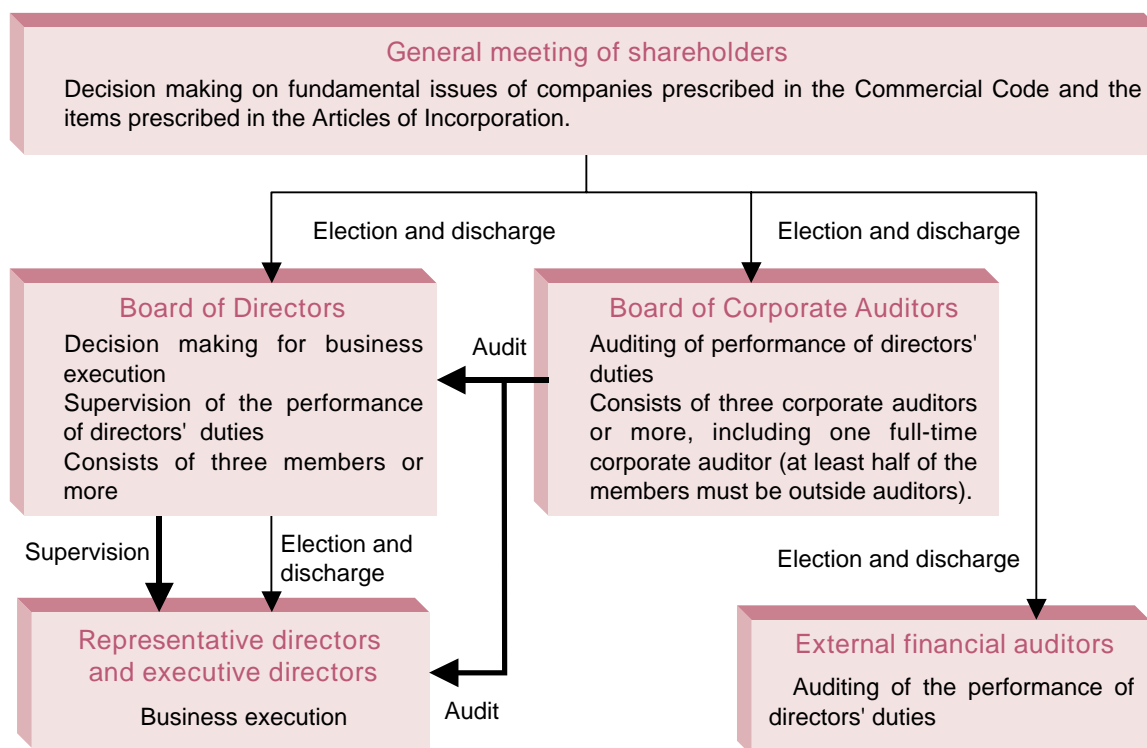
Three committees must be established in a company with a committees system: a nomination committee, an audit committee and a compensation committee (each committee should be made up of three or more directors, and at least half of the members of each committee should be outside directors). The nomination committee is given the authority to determine the agenda concerning the election and discharge of directors submitted to the general meetings of shareholders, the audit committee must audit the performance of duties of directors and executives, and the compensation committee is given the authority to determine the compensation for individual directors and executive officers. Executive officers who serve as a business execution body must be appointed, and the representative executive officers of such executive

officers serve as a company representative body.

(*1) The committees system is a system that was introduced in April 2003 when the Commercial Code was amended. Before such amendment, only the corporate auditor system existed.

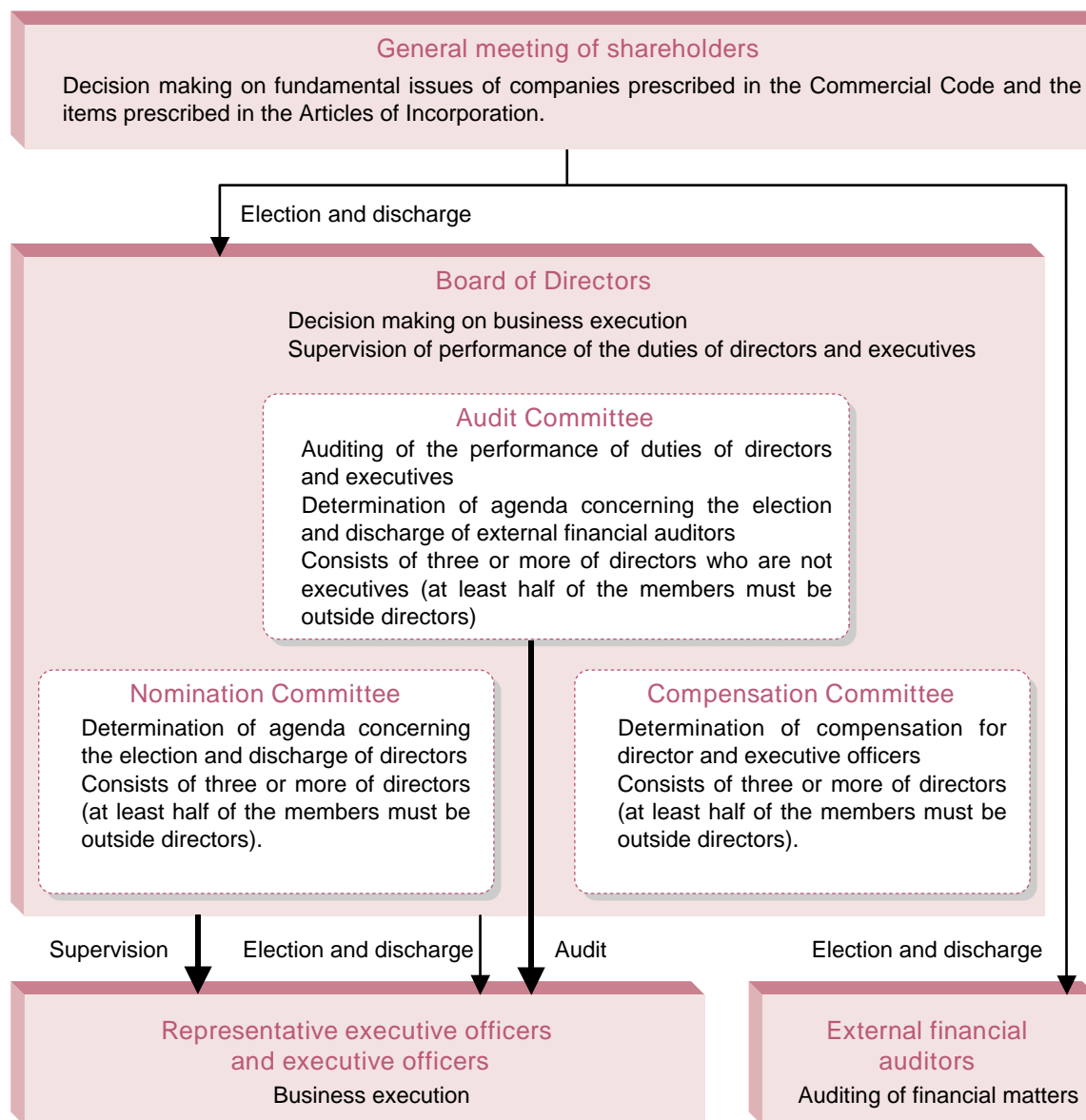
(*2) With respect to companies with a corporate auditors system, outside auditors must be nominated, but the appointment of outside directors is not required.

Companies with a Corporate Auditors System



- * The terms of office for directors and corporate auditors are two years and four years, respectively.
- * Corporate auditors are not allowed to additionally assume the positions of directors or employees of the company or any of its subsidiaries.
- * Outside auditors are limited to those who are not, and were not directors or employees of the company or any of its subsidiaries.
- * Corporate auditors must attend the meetings of the board of directors and express their opinions as the occasion demands.
- * When a director intends to submit an agenda concerning the election of any corporate auditor, that director must obtain the consent on such submission from the board of corporate auditors.
- * At the general meetings of shareholders corporate auditors may express opinions on the election or discharge of any corporate auditor.
- * When a director intends to submit an agenda concerning the election or discharge of any external financial auditor, that such director must obtain the consent of such submission from the board of corporate auditors.

Companies with a Committees System



* The terms of office for directors and executive officers shall be one year (unlike companies with a corporate auditors system, companies that have a committees system must annually entrust directors through the general meetings of shareholders since the authority of the definitive plan for distribution of profit is given to the board of directors instead of the general meetings of shareholders).

* Directors are not allowed to execute the business of the company (however, directors can be

executive officers).

* Members of the nomination committee, audit committee and compensation committee are elected by the board of directors.

* Outside directors are directors who are not executive officers of the company, were not executive directors or executive officers of the company or any of its subsidiaries in the past, and currently are not executive directors or executive officers of any of its subsidiaries nor employees of the company or any of its subsidiaries.



Report on Enhanced Corporate Governance for Listed Companies



2004.3.11

Listed Company Corporate Governance Committee

Enhanced Corporate Governance for Listed Companies Report of the Listed Company Corporate Governance Committee

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Vice-Chairman

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Takeshi Yoshii Senior Corporate Auditor, Nippon Steel Corporation

In response to the request of the late Mr. Masaaki Tsuchida, former President and CEO of Tokyo Stock Exchange, Inc., the Listed Company Corporate Governance Committee commenced its discussions on December 24, 2002.

Mr. Tsuchida's vision was that Tokyo Stock Exchange play a more proactive role than ever before in enhancing the corporate governance of listed companies, thereby deepening the mutual understanding among listed companies, shareholders, and investors, attracting more interest in investing in listed companies, and enhancing confidence in Tokyo Stock Exchange as a global capital market.

Since then, the Listed Company Corporate Governance Committee conducted twelve meetings over a period of three years, in the course of which this report was compiled.

The deliberations began with basic issues, such as how to define the concept of corporate governance and where its objectives lie. Next, the Committee proceeded to the deliberation of fundamental issues relating to corporate governance, and later, to the role that Tokyo Stock Exchange should play to enhance it. Each deliberation was very active and invariably required more time than had been allotted.

The following pages give a concise summary of the background behind the Committee's deliberations and their conclusions.

Amidst the global development of businesses and access to global capital markets by listed companies, and changes in the structure of shareholders - most notably, the elimination of cross shareholdings and the appearance of more shareholders demanding their rights - recent years have seen more and more listed companies making voluntary efforts to enhance their corporate governance.

Additionally, in parallel with these efforts, basic legislations and legal bases in relation to corporate governance have rapidly been developed and improved. Pursuant to the Commercial Code, listed companies are now granted various options and a freer environment in which to attain enhanced corporate governance, including the introduction of a committees system, a corporate auditor system with reinforced principal power of corporate auditors, etc. In terms of the Securities and Exchange Law, following the establishment of a mandatory system to disclose information relating to corporate governance as demanded in the preliminary release of performance results by Tokyo Stock Exchange last year, information disclosure relating to corporate governance in securities reports is to become mandatory, and the accountability of individual listed companies is

certain to be an important part of evaluation by the market.

In light of the rationale mentioned above, much active discussion led the Committee to reach an agreement on the following two issues.

Firstly, corporate governance should be enhanced as individual listed companies search for methods of corporate governance suitable for their own operations by freely adopting various options, and entrusting those methods to shareholders and investors in their evaluation of the market. Secondly, Tokyo Stock Exchange should not regulate listed companies in terms of corporate governance or induce compliance, but rather should compile a set of disciplines and principles relating to corporate governance to assist shareholders and investors in their evaluation of the market, and provide them as a basis of common recognition between all concerned parties.

Based on these agreements, the Committee compiled the attached "Principles of Corporate Governance for Listed Companies," a list of principles and disciplines relating to corporate governance that the Committee recommends Tokyo Stock Exchange to provide to concerned parties.

These Principles of Corporate Governance for Listed Companies have been agreed upon as the result of sincere discussions undertaken by Committee members of different standpoints. In the course of discussion, all Committee members have strived to reach a common understanding and thereby overcome the large divergence of opinions.

The Committee requires Tokyo Stock Exchange to adopt these Principles of Corporate Governance for Listed Companies and disseminate them thoroughly to concerned parties including listed companies, shareholders, and investors. In this way, these Principles of Corporate Governance for Listed Companies are to be utilized for the enhancement of listed companies' accountability, the enhancement of corporate governance based on the evaluation of the market, and related information disclosure. In addition, the Committee demands that Tokyo Stock Exchange convey the nature of the Principles of Corporate Governance for Listed Companies widely throughout the world and make known the sincere efforts that have been undertaken for corporate governance in its market.

Finally, please note that the agreements made at the Committee, especially those relating to the expected roles of Tokyo Stock Exchange, have been reached as a result of extremely active discussions by all the Committee members.

Some members have held from the outset that some guidelines for corporate governance should be determined with respect to the disclosure of governance-related information in the preliminary release of financial results, with which listed companies should be required to comply. Further, that disclosure practices should be enhanced by adopting a method whereby listed companies are requested to enter "comply or explain" on their statements so that any contravention of the guidelines that have taken place are disclosed and explained. However, others have argued that, considering that only one year has elapsed since the establishment of the mandatory system to disclose information relating to corporate governance in the preliminary release of financial results, and the disclosure of corporate governance information in the securities report pursuant to the Securities and Exchange Law is about to be implemented, the measures mentioned above would be premature. In addition, others argued that listed companies have just started considering a governance system suitable for themselves, and that measures that might induce corporate governance to move in a certain direction should be avoided. Consequently, no agreement has been reached on the disclosure of governance-related information in the preliminary release of financial results.

This report has presented recommendations regarding new steps that Tokyo Stock Exchange should take to enhance the corporate governance of listed companies. As indicated by the proceedings of these discussions, the roles required of Tokyo Stock Exchange are likely to be reviewed amidst the ever-changing conditions surrounding corporate governance. The Committee concluded that Tokyo Stock Exchange should continue to review its tackling of this issue.

This Committee was launched in 2002 with Mr. Nobuo Tateishi, Chairman and Representative Director of Omron Corporation (-his title at that time; Mr. Tateishi is currently an advisor), appointed as the Committee chairman. The Committee expresses its special appreciation for his management of the Committee proceedings during his former posting and for his invaluable support thereafter. The Committee would also like to express its appreciation to Mr. Atsushi Murayama, the former Executive Vice President of Matsuhita Electric Industrial Co., Ltd. (currently Representative Director of Kansai International Airport), and Mr. Takushi Shimoda, the former Managing Director of Tokyo Stock Exchange (currently Senior Managing Director of the Association of Tokyo Stock Exchange Regular Members), both of whom have retired from the Committee.

In addition, the Committee would like to express its deep gratitude to the representatives from the Financial Services Agency, Ministry of Justice, Ministry of Foreign Affairs, Ministry of

Finance, Ministry of Economy, Trade and Industry and Japan Securities Dealers Association, who have supported the Committee as observers, and to the members of the sub-committees who participated in the determination of issues for deliberation.

Finally, the Committee would like to express its condolences to the family of Mr. Masaaki Tsuchida, a keen participant in the discussions at the Committee, who passed away on January 30, 2004 without seeing this report.

Proceedings

First round:	December 24, 2002
Second round:	January 22, 2003
Third round:	February 14, 2003
Fourth round:	May 5, 2003
First sub-committee:	March 20, 2003
Second sub-committee:	April 8, 2003
Fifth round:	April 30, 2003
Sixth round:	May 21, 2003
Seventh round:	June 18, 2003
Eighth round:	September 24, 2003
Ninth round:	October 22, 2003
Tenth round:	November 21, 2003
Third sub-committee:	December 3, 2003
Fourth sub-committee:	December 18, 2003
Eleventh round:	February 4, 2004
Twelfth round:	February 20, 2004

The English language translation of "Principles of Corporate Governance for Listed Companies" and "Report on Enhanced Corporate Governance for Listed Companies" was prepared by I.S.S. Inc.



Tokyo Stock Exchange, Inc.
Listing Department

2-1 Nihombashi-Kabuto-cho
Chuo-ku, Tokyo 103-8220, Japan
URL: <http://www.tse.or.jp/>

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