

# Corporate Governance

- ISO 26000: Organizational governance -

## Basic approach

The Hodogaya Chemical Group strives to create values for the various stakeholders including our shareholders, customers, partner companies, local communities, and employees; contribute to the development of domestic and global economies and industries for the prosperity of society; ensure the soundness and legality of management; and increase efficiency, all the while steadily supplying “Only One/Number One” specialty products in the global and niche markets. We have established these targets as highest priority of management as we work toward enhancing and strengthening our corporate governance system.

## Corporate governance system

Aiming to ensure the effectiveness of our corporate governance and to improve our corporate value, Hodogaya Chemical made a transition to a “Company with an Audit & Supervisory Committee” structure in June 2015, to further strengthen the Board of Directors’ supervisory functions with the participation of Outside Directors.

To increase the speed and agility of corporate management, Directors are entrusted with the decision-making on all business operation matters other than matters that should be solely for the Board of Directors to determine as required by laws and regulations. Meanwhile, Directors report the performance of their duties to the Board of Directors, as well as mutually monitor and supervise the performance of duties with other Directors. The Audit & Supervisory Committee supports the supervisory functions of the Board of Directors, and evaluates the

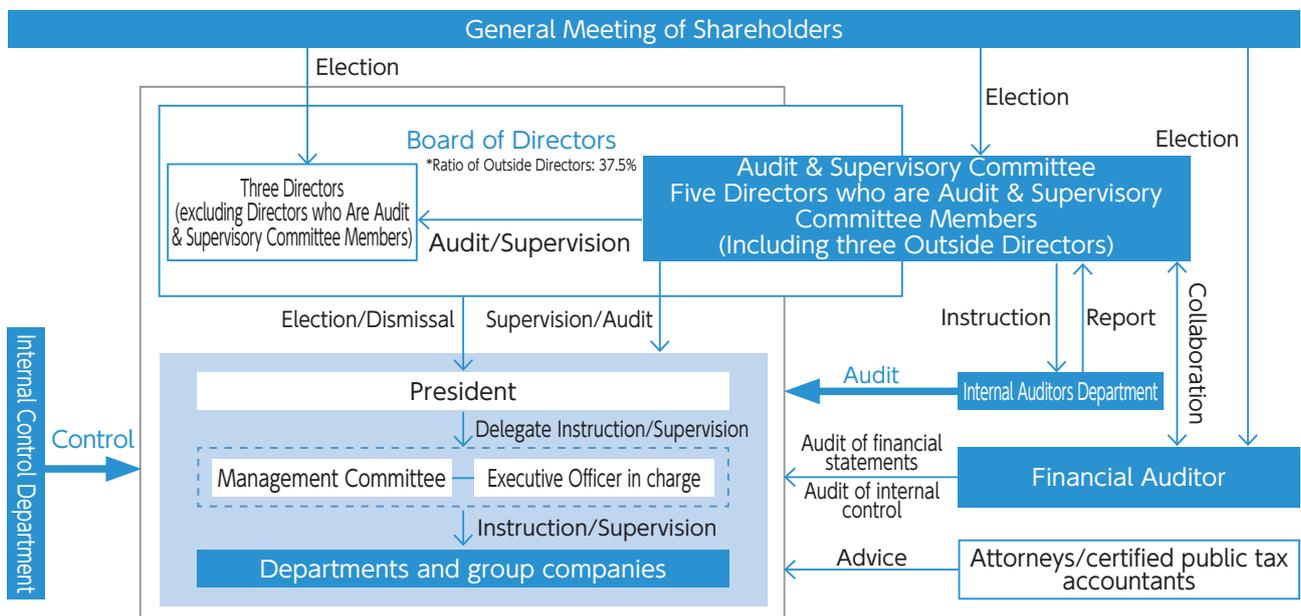
Board of Directors by assessing mainly such items as to whether the Board of Directors is conducting thorough discussions on the appropriate agenda items based on its role, and whether a sufficient support system is in place to enhance the content of discussions at the Board of Directors’ meeting.

Additionally, in January 2018, the Company shifted into a new management structure which facilitates separation of the “strategic decision-making and supervisory functions of management” from the “prompt executive functions of business strategy,” with a view to further strengthen its supervisory and executive functions. As a result, the number of Directors who are not Audit & Supervisory Committee Members has been reduced from seven to three. Accordingly, the ratio of Outside Directors is now 37.5%.

### Initiatives to strengthen corporate governance

June 2003	Introduction of executive officer system
March 2004	Abolishment of directors’ retirement benefits program
May 2006	Formulation of Basic Policy on Internal Control
November 2006	Establishment of Internal Control Department
June 2013	Start of appointment of Outside Directors
June 2015	Transition to a Company with Audit & Supervisory Committee
July 2016	Introduction of stock-based compensation plan
January 2018	Shift into new management structure

### Structure of corporate governance system



● **General Meeting of Shareholders** .....

In addition to the appropriate statutory disclosure and timely disclosure, Hodogaya Chemical strives to proactively provide shareholders and investors with relevant information such as its management strategies, in order to gain understanding on its business activities. It also establishes measures to encourage shareholders to attend the General Meeting of Shareholders. It engages in constructive bilateral dialogue with shareholders in an effort to achieve effective corporate governance that can contribute to sustainable growth of Hodogaya Chemical and increase its corporate value.

● **Board of Directors** .....

To enable thorough discussions based on diverse opinions and prompt, rational decision-making, the Board of Directors consists of a total of eight Directors, including “Directors (excluding Directors who are Audit & Supervisory Committee Members)” and “Directors who are Audit & Supervisory Committee Members.” Sets of criteria for the election of Directors are established. Among other things, an Internal Director should have the personality, extensive experience, and quality to appropriately serve as a corporate manager, and an Outside Director should have appropriate experience and knowledge cultivated by broad business experiences. At Hodogaya Chemical, those who are considered to possess these qualities are reviewed and nominated as candidates for Directors by the Board of Directors. Reasons for nomination as candidates for Directors, including career summary, are published in the Reference Documents for General Meeting of Shareholders which can be found on our corporate website.

● **Audit & Supervisory Committee** .....

The Audit & Supervisory Committee consists of five Directors (including three Outside Directors), and audits the legality of business execution by Directors and officers, appropriateness of the Company’s business operations, internal control, and financial status, etc. by attending important meetings and ordering timely and appropriate reporting from Directors, Executive Officers and employees of the Hodogaya Chemical Group. The Audit & Supervisory Committee also maintains close relations with the Financial Auditor to take necessary measures in relation to the audit work.

● **Executive Officer** .....

The executive officer system of Hodogaya Chemical was introduced in view to (1) streamline management, (2) as a result enable quicker decision-making, (3) specialize functions, (4) strengthen supervisory and monitoring functions, and (5) strengthen our business management. Executive

Officers who can fulfill these goals have been elected by President to execute the business of our core departments.

● **Financial Auditor** .....

Hodogaya Chemical appoints Grant Thornton Taiyo LLC as its Financial Auditor, and in addition to financial audit services, receives advices on accurate and fair business practices through internal control audit.

● **Internal Control Department** .....

Hodogaya Chemical has the Internal Control Department that continuously reviews and evaluates that a group-wide internal control systems required under the Companies Act and the Financial Instruments and Exchange Act are in place and implemented, and ensures that any existing business risks are maintained lower than the predetermined level. We maintain and strengthen the level of our group-wide internal control, and promote various policies to ensure that our business operations are conducted in an appropriate and effective manner.

● **Internal Auditors Department** .....

Hodogaya Chemical has the Internal Auditors Department that monitors our internal control system in accordance with the Companies Act, etc., and ensures the appropriateness of our business operations. It also serves as the secretariat of the Audit & Supervisory Committee and supports the Committee’s operation and helps maintain and improve the audit quality.

● **Directors’ compensation** .....

The amount of remuneration of Directors are determined within the maximum limit of remuneration approved at the General Meeting of Shareholders, taking into consideration factors such as the performance of the Company, standard amounts of directors’ compensation, and consistency with the salaries of Executive Officers and employees. Since FY2016, Hodogaya Chemical has introduced a “stock-based compensation plan” for Directors (excluding Directors who are Audit & Supervisory Committee Members) and Executive Officers with the objective to raise awareness to contribute to improve performance for the mid- to long-term of the Hodogaya Chemical Group and increase its corporate value. This “stock-based compensation plan” is an officer incentive program in which the Group issues stocks (treasury shares) of Hodogaya Chemical to its officers based on the positions held and level of achievement of performance goals as well as their level of contribution to achieving Hodogaya Chemical’s mid-term management plan “HONKI 2020.”

► Risk management

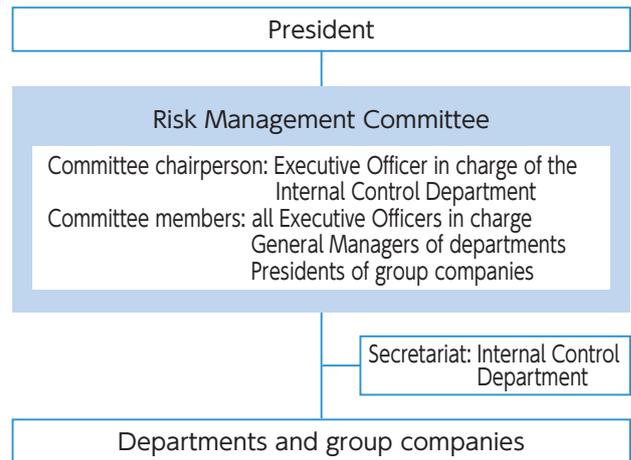
● Basic approach

The Hodogaya Chemical Group has its own risk management system in place to minimize damages associated with illegal acts against the Group, quality issues, natural disasters and other risks. In order to maintain and increase corporate value, to fulfill corporate social responsibilities, and to achieve sustainable growth of the Group, all officers and employees are engaged in initiatives to increase risk awareness and promote risk management.

● Risk Management Committee

Hodogaya Chemical has a Risk Management Committee in place, in accordance with the Risk Management Committee Rules. The Committee holds regular meetings to share risk awareness, develop measures to reduce risks, review the progress of such measures, and take initiatives to minimize damages, on a group-wide basis, in accordance with the Crisis Management Rules. As for information securities, we are formulating internal rules and regulations to store and manage information appropriately, and conducting educational activities such as the compliance training.

■ Risk management structure



► Compliance

● Promotion structure

The Hodogaya Chemical Group formulates various rules and regulations based on the Basic Policy on Internal Control, and strives to achieve compliance through organized and cross-sectional initiatives led by the Internal Control Department. The Internal Auditors Department audits the status of compliance and provides advice and guidance for improvements if necessary.

● Corporate Code of Conduct, Compliance Action Policy

Hodogaya Chemical has formulated the Corporate Code of Conduct, the Compliance Action Policy, and other compliance-related policies and rules. All officers and employees of the Hodogaya Chemical Group abide by these rules and act in accordance with laws and regulations, the company’s Articles of Incorporation, and the social norms. The Corporate Code of Conduct sets forth the guiding principle that the companies, officers and employees must follow in all corporate activities undertaken by the Hodogaya Chemical Group. The Compliance Action Policy clarifies in a more comprehensible manner the Corporate Code of Conduct which sets forth the matters that must be observed in executing operation, based on the understanding that it is essential for the sound development of the Hodogaya Chemical Group for all of its officers and employees to have complete understanding of the social responsibilities of the Group, to ensure full compliance of relevant laws and regulations and internal rules in all aspects of corporate activities, and to behave in accordance with the social norms.

● Tax compliance

The Hodogaya Chemical Group will respond to the social demands and expectations by duly fulfilling its tax obligation in each country and region, as stipulated in the Corporate Code of Conduct and the Compliance Action Policy.

To do so, we work to maintain and improve tax compliance through actions such as formulating structures to accommodate various taxation systems, cooperating in submitting tax information to the tax authorities in a timely and appropriate manner, and not engaging in intentional tax avoidance through income transfer to other countries or the use of tax haven.

## ● Internal reporting system

The Hodogaya Chemical Group has set up an internal reporting system under its Internal Reporting Rules in order to ensure early detection and prevention of violations of laws and business ethics. Reports are received by the Internal Control Department and outside legal consultants. The system ensures that, in conducting investigations based on reports, the privacy of the reporters and the secrecy of the content of their report are protected to the maximum extent possible. The protection of reporters is clearly stipulated in the Internal Reporting Rules and utmost care is given so that a reporter with honest intentions do not receive any disadvantageous treatment such as dismissal, displacement, or discrimination as a result of their reporting.

## ● Compliance education

In terms of cultivating and improving compliance awareness, the Hodogaya Chemical Group continuously offers compliance training sessions and independent education using e-Learning for all Group officers and employees, in order to thoroughly ensure compliance.

In addition, officers and managerial personnel of the Group are required to take the Examination of Compliance Proficiency for Practical Business (Primary Level) to gain knowledge and increase understanding of compliance.

## Criteria for independence of Outside Directors

At Hodogaya Chemical, candidates for independent outside directors are selected from among those who meet the Tokyo Stock Exchange's requirements of independence and possess extensive experience and knowledge.

Accordingly, the Company has registered three of the Outside Directors as independent officers specified by the Tokyo Stock Exchange, and if the Substitute Director Who Is an Audit & Supervisory Committee Member is appointed as Director, the Company intends to register him as independent officer specified by the exchange.

Note that one of the Outside Directors and the Substitute Director Who Is an Audit & Supervisory Committee Member had been employees of a financial institution which is a major lender to the Company; however, nine years have elapsed since they left said financial institution. Therefore, the Company deems that there are no concerns over their independence.

### Voice



Legal Department  
Attorney Masayuki Kamigauchi

### Everything begins from information gathering

Every task at the Legal Department begins by gathering information. We cannot draft an appropriate contract unless we understand the laws and regulations and rulings that serve as precedents to the objectives we want to achieve. Handling legal disputes is also part of our job, and my experience as an attorney has helped me gain some insight on how to resolve disputes.

Highly accurate information is essential in delivering quality results, but since the rules such as laws, regulations and precedents are changing every day together with the change in society, I try to keep my knowledge updated at all times. Corporate governance cannot be enhanced and strengthened unless not only the Legal Department but also all employees implement it, recognizing its importance, so I am hoping to support this initiative through my daily work.