Vanguard funds

Proxy voting policy for Japanese portfolio companies

Effective March 1, 2023

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Introduction

The information below, organized according to Vanguard Investment Stewardship's four principles, is the voting policy for Japanese-domiciled companies and details the general positions of the Vanguard-advised funds (the "Funds' Boards")[1] on proxy proposals presented for shareholders to vote on.

It is important to note that proposals often require a facts-and-circumstances analysis based on an expansive set of factors. Proposals are voted case by case under the supervision of the Investment Stewardship Oversight Committee and at the direction of the relevant Fund's Boards. In all cases, proposals are voted as determined in the best interests of each fund consistent with its investment objective.

Companies should abide by the relevant local laws and regulations of the market in which they are listed and follow any applicable local corporate governance codes and best practices. These local corporate governance codes form the basis of the funds' country-specific guidelines. However, they may differ and, in some cases, require a higher level of governance best practice than the local corporate governance code.

Comply or explain. Local standards in Japan permit companies to deviate from recommended corporate governance practices as long as they provide an explanation for the deviation. The Companies Act and the Listing Rules provide the primary legislative framework for Japanese corporate governance, with best practices outlined in Japan's Corporate Governance Code operating on a comply-or-explain basis. Vanguard supports this underlying principle of corporate governance best practice. Companies should explain any deviations from recommended governance practices, including providing an explanation of what they do instead of the recommended practice and why their alternative systems and/or processes are in the best interests of shareholders.

Multijurisdictional companies. When a company is listed on multiple exchanges or incorporated in a country different from where it is listed, the company should follow the applicable laws and listing rules of the market(s) in which it has its primary listing and apply any local corporate governance codes. If a company deviates from any market standards or local corporate governance codes, it should explain the reasons for such deviations.

1 This voting policy details the general positions of the funds for each portfolio advised by Vanguard, including Vanguard index funds and ETFs and the fund assets managed by Vanguard Quantitative Equity Group ("Vanguard-advised funds"), on recurring proxy proposals for Japanese-domiciled companies. Each of the U.S. mutual funds advised by Vanguard retains proxy voting authority, and this voting policy reflects the U.S. Fund Board's instructions governing proxy voting by the Vanguard-advised funds.

Principle I: Board composition and effectiveness

The funds' primary interest is to ensure that the individuals who represent the interests of all shareholders are independent, committed, capable, diverse, and appropriately experienced. Diversity of thought, background, and experience, as well as of personal characteristics (such as gender, race, ethnicity, and age), meaningfully contribute to a board's ability to serve as effective, engaged stewards of shareholders' interests.

Board independence

In Japan, corporate law allows for three types of company board structures:

1. A one-tier board with three committees (audit, nominating, and compensation).

2. A one-tier board with an audit committee.

3. A two-tier board (board of directors and a board of statutory auditors).

The funds believe the company is best positioned to choose which type of board structure is best suited to oversee the risks and opportunities it is facing and therefore do not advocate for a particular structure.

In line with the Japanese Corporate Governance Code, for Prime listed companies without a controlling shareholder, a fund will generally vote against top management, or other relevant directors responsible for appointing board members, if the board is composed of less than one-third independent outside directors.

For Prime listed companies with a controlling shareholder, a fund will generally vote against top management, or other relevant directors responsible for appointing board members, if the board is not composed of majority independent outside directors.

For all other listed companies without a controlling shareholder, a fund will generally vote against top management, or other relevant directors responsible for appointing board members, if there are fewer than two independent outside directors on the board.

For all other listed companies with a controlling shareholder, a fund will generally vote against top management, or other relevant directors responsible for appointing board members, if the board is composed of less than one-third independent outside directors.

Outlined below are common factors that can affect independence:

- *Current and former employees.* Individuals who are current or former employees will generally not be considered independent.
- *Cross-directorships.* Any directors who hold cross-directorships or have significant links with other directors through involvement in other companies or bodies will generally not be considered independent. In addition, directors who work at companies considered "cross-shareholdings" of the company in question generally will not be considered independent.
- *Shareholder representatives.* Representatives of shareholders or those who work at shareholders will not generally be considered independent. In addition, any directors who have a close familial relationship and/or business connection (see definition below) to a shareholder will not generally be considered independent.
- *Business connections.* Any director nominee who has had a material business relationship with the company, either directly or as a partner, shareholder, director, or senior employee of a body that has such a relationship with the company, will generally not be considered independent.
- *Familial relationship and other personal relationships.* Any director who has close family ties with any of the company's advisors, directors, or senior employees will generally not be considered independent.
- *Performance-related pay.* Any director who participates in a performance-related pay scheme will not generally be considered independent.
- *Other factors.* If it is determined, through engagement or research, that director independence has been compromised, that director may not be considered independent.

Key committee independence

For a one-tier board with three committees or an audit committee, a fund will generally vote against inside directors and/or nonindependent outside directors if the key committee(s) (the audit, nomination, and/or remuneration committees) is (are) not composed of majority independent directors.

Board chair independence

Generally, a fund will vote for management proposals to create an independent chair position or to otherwise separate the CEO and Chair positions.

In evaluating shareholders proposals calling for the separation of the CEO and chair, certain factors are considered:

- *Presence of a lead/senior independent director role.* A strong lead/senior independent director may provide sufficient independent perspective to balance against a nonindependent chair. Consistent with this perspective, structures that do not provide a strong counter-voice to insider leadership warrant independent oversight.
- *Board accessibility.* Shareholders' ability to communicate directly with independent outside directors, including a lead/senior independent director or committee chairs, is an important means by which they can share their perspectives. Restricting access to independent outside directors may prevent the board from receiving comprehensive and understanding feedback from shareholders to incorporate into corporate practices. It may also contribute to a culture of management entrenchment by controlling the messages the board receives.
- *Overall board independence.* High affiliated representation on the board may outweigh independent voices and further entrench the insider leadership. Enhancing the role of independent outside directors may offer a counterweight to the nonindependent voices on the board.
- *Governance structural flaws.* Certain governance practices and corporate structures may make entrenchment by management and other nonindependent board directors more likely.
- *Responsiveness to shareholders.* A pattern of being unresponsive to shareholders (e.g., a failure to act on shareholder votes or decision to impair shareholder rights) may indicate that a board is entrenched. A stronger independent leadership role may be necessary to remedy this.
- *Oversight failings.* Governance crises may indicate management entrenchment or that the board is not receiving sufficient information from management to appropriately fulfill its oversight role. Evidence of failure to provide appropriate governance oversight, and/or evidence of failure to oversee material or manifested risks, including those that may be considered environmental or social, will be taken into account.

Election of statutory auditors

The funds evaluate the independence of statutory auditors using the same independence criteria above for directors.

A fund will generally vote against the election of nonindependent statutory auditors if the statutory audit board is not majority independent.

A fund will generally vote against statutory audit board nominees if they attended less than 75% of board and/or statutory audit board meetings.

A fund will generally vote against statutory audit board nominees if there are concerns related to a material financial misstatement or fraud and the nominee is judged to be responsible for any mismanagement associated with it.

Diversity and qualifications

Well-composed boards, in addition to having appropriate independence, should have skills and perspectives that are informed by a range of backgrounds, experience, and personal characteristics.

The Vanguard funds look for regular board effectiveness reviews and subsequent refreshment of board composition to suit the company's long-term strategy, business model, and market environment. Considerations should include independence, skills/experience gaps, and the diversity of the board.

We have long recognized the importance of diversity in the boardroom. Diverse individuals both personally and professionally bring unique experiences and perspectives that help challenge, debate, and meaningfully contribute to a board's ability to serve as effective, engaged stewards of shareholders' interests within the boardroom.

The Vanguard funds look for companies to meet local market standards related to board composition and diversity, and at a minimum, for TOPIX100 companies to demonstrate progress toward gender diversity on the board.

We ask that companies disclose a "skills matrix" to allow shareholders to assess the overall board composition, and how well-suited individual director nominees are to support and oversee the company's evolving business strategy and risks.

We look for boards to consider and disclose, in accordance with local law and best practice guidance, the diversity of existing board members and proposed nominees on factors such as background, skills, gender, age, race, ethnicity, and national origin, at least on an aggregate basis. Companies that do not have diverse boards should:

- Demonstrate a commitment to achieving board diversity through robust nomination processes;
- Provide insights on progress against internal targets, policies and practices; and
- Prioritize adding diverse voices to their boards.

Director attendance

A fund will generally vote against directors and statutory auditors who attended fewer than 75% of board meetings in the previous year unless an acceptable extenuating circumstance is disclosed.

We note that sometimes companies do not disclose the meeting attendance for insiders on the board. We encourage companies to disclose the meeting attendance for all directors.

Director liability

A fund will vote case by case for management proposals to limit directors' liability and to expand indemnity provisions.

In general, a fund will vote for proposals to indemnify directors for breach of fiduciary duty of care as long as the director is found to have acted in good faith and will vote against proposals to indemnify directors for activity involving willful breach of fiduciary duties or other criminal activity.

Directors' names and biographies

A fund will generally vote against any director whose name and biographical details have not been disclosed sufficiently in advance of the general meeting.

Escalation process: Director and committee concerns

In certain instances, a fund may vote against a director as a means to express concerns regarding governance failings or other issues that remain unaddressed by a company.

- *Oversight failure.* A fund will generally vote against directors who have failed to effectively identify, monitor, and manage material risks and business practices that fall under their purview based on committee responsibilities, including, but not limited to, social and environmental risks. In cases where a specific risk does not fall under the purview of a specific committee, a fund will generally vote against the chair, lead independent director, most senior executive director, or any relevant director(s). See page 9 for more detail on the consideration of risk oversight failures.
- *Lack of board diversity.* Absent a compelling reason, for TOPIX100 companies, a fund may vote against the re-election of members of the nomination committee if relevant given the board structure, chair, lead independent director, and/or the most senior executive director if there are no women on the board.
- *Egregious pay practices.* A fund may vote against the remuneration committee chair if relevant given the board structure, chair, lead independent director, most senior executive director, and/or any relevant director(s) when the company exhibits egregious pay practices but a pay-related resolution is not on the general meeting's agenda.
- *Limited shareholder rights.* A fund may vote against the chair, lead independent director, most senior executive director, and/or any relevant director(s) if the company has abused minority shareholder rights and/or has somehow meaningfully limited shareholder rights, including the adoption or renewal of a poison pill (anti-takeover/defense plan) without presenting it for a shareholder vote.
- *General egregious practices.* A fund may vote against the chair, lead independent directors, most senior executive director, and/or any relevant director(s) if it deems that there are material failures of governance, stewardship, and/or fiduciary responsibility at the company.

Generally, a fund will vote for new directors who would otherwise fail under any of the preceding circumstances regarding committee accountability but have served for less than a year unless a director fails to carry out the basic responsibilities that would be expected even for a new director.

Contested director elections

A fund will vote case by case on shareholder nominees in contested director elections. The analysis of proxy contests focuses on three key areas:

- *The case for change at the target company*
  - How has the company performed relative to its peers?
  - Has the current board's oversight of company strategy or execution been deficient?
  - Is the dissident focused on strengthening the target company's long-term strategy and shareholder returns?
- *The quality of the company and dissident board nominees*
  - Is there reason to question the independence, engagement, or effectiveness of the incumbent board?
  - Has the board delivered strong oversight processes with long-term shareholders' interests in focus?
  - Are the directors proposed by the dissident (whether the full slate or a subset) well-suited to address the company's needs, and is this a stronger alternative to the current board?
- *The quality of company governance*
  - Did the board engage in productive dialog with the dissident?
  - Is there evidence of effective, shareholder-friendly governance practices at the company?
  - Has the board actively engaged with shareholders in the past?

Principle II: Oversight of strategy & risk

Boards are responsible for effective oversight and governance of the risks most relevant and material to each company and for governance of the company's long-term strategy. They should take a thorough, integrated, and thoughtful approach to identifying, quantifying, mitigating, and disclosing risks that have the potential to affect shareholder value over the long term. Boards should communicate their approach to risk oversight to shareholders through their normal course of business.

Capital structures

- *Dividends*. A fund will generally vote for proposals to allocate income unless aware of an egregious reason why a fund should not support management's proposal.
- *Share issuance requests*. The total dilution to existing shareholders and the company's history of issuing capital will be considered.
  - A fund will generally vote for an increase to authorized capital as long as it does not exceed 100% of the current authorized capital and the company provides an adequate rationale for the increase.
  - A fund will generally vote on case by case on the issuance of shares to a third party and/or for a private placement, considering the rationale and the terms and conditions of the transaction.
- *Share repurchase and reduction of capital*. A fund will typically vote for routine authorities to repurchase shares up to 10% of the current issued share capital as long as the terms of the repurchase appear to be in the best interests of shareholders and there is no history of abuse of such authorizations.
  - A fund will vote case by case on amendments to company articles that give the board discretion to initiate share repurchases without prior shareholder approval, taking into account the rationale provided and past share repurchases and dividend payouts.
  - A fund will vote case by case on shareholder proposals requesting the company to engage in share repurchases, reduction of capital, or other specific capital- related transactions if there are concerns pertaining to corporate malfeasance, unfavorable behavior, or relative company performance.
- *Preferred stock*. A fund will typically vote case by case on proposals to create/amend/issue preferred stock, taking into account the reason for the issuance, the ownership profile of the company, any historical abuses of share issuances, and the company's general approach to shareholder rights.

Mergers, acquisitions, and financial transactions

A fund will vote case by case on all mergers, acquisitions, and financial transactions.

A fund seeks to assess the likelihood that a transaction preserves or will create long-term value for shareholders. A fund's evaluation of each transaction is governance-centric and focuses on four key areas:

- Valuation
- Strategic rationale
- Board oversight of the deal process
- The surviving entity's governance profile

In evaluating board oversight, the fund will consider independence, potential conflicts of interest, and management incentives.

Appointment of audit firm

A fund will generally vote for the appointment of the proposed audit firm unless there are serious concerns related to changing auditors or the new auditor's independence is compromised.

Environmental/social proposals

Disclosure proposals

A fund will vote on case by case on disclosure-related management and shareholder proposals based on the materiality of environmental and social risks to a company.

Clear, comparable, consistent, and accurate disclosure enables shareholders to understand the strength of a board's risk oversight. Because sustainability disclosure is an evolving and complex topic, a fund's analysis of related proposals aims to strike a balance in avoiding prescriptiveness and providing a long-term perspective.

Targets, policies, and practices proposals

Similarly, a fund will vote case by case on management and shareholder proposals that request adoption of specific targets or goals and on proposals that request adoption of environmental or social policies and practices.

Shareholders typically do not have sufficient information about specific business strategies to propose specific targets or environmental or social policies for a company, which is a responsibility that resides with management and the board. As a result, shareholder proposals that are more prescriptive in nature will generally not be supported by a fund.

Considerations for environmental and social proposals

Each proposal will be evaluated on its merits and in the context that a company's board has ultimate responsibility for providing effective oversight of strategy and risk management. This oversight includes material sector- and company-specific sustainability risks and opportunities that have the potential to affect long-term shareholder value.

While each proposal will be assessed on its merits and in the context of a company's current practices and public disclosures, vote analysis will also consider these proposals relative to market norms or widely accepted frameworks endorsed or already referenced by Vanguard's Investment Stewardship program. Input from the board, management, and proponents may also be taken into consideration. To assist companies in understanding relevant principles, research, or past voting decisions, Vanguard will from time to time publish perspectives on notable issues and best practices for companies to consider on specific environmental or social matters.

A fund may support shareholder proposals that:

- Address a shortcoming in the company's current disclosure relative to market norms or to widely accepted frameworks endorsed or referenced by Vanguard's Investment Stewardship program (e.g., the Sustainability Accounting Standards Board, the Task Force on Climate-related Financial Disclosures);
- Reflect an industry-specific, materiality-driven approach; and
- Are not overly prescriptive in dictating company strategy or day-to-day operations, or about time frame, cost, or other matters.

If the above criteria are met, a fund may support the following types of proposals:

Specific to environmental proposals (not exhaustive):

- Request disclosure related to companies' Scope 1 and Scope 2 emissions data, and Scope 3 emissions data in categories where climate-related risks are deemed material by the board.
- Assessment of the climate's impact on the company, disclosing appropriate scenario analysis and related impacts to strategic planning.

Social risk proposals (not exhaustive):

- Request disclosure on workforce demographics inclusive of gender and racial/ethnic categories, considering other widely accepted industry standards, and if appropriate under applicable laws and regulations. This could include publishing EEO-1 reports.
- Request disclosure on the board's role in overseeing material diversity, equity and inclusion (DEI) risks or other material social risks.
- Request the disclosure of the company's approach to board composition, inclusive of board diversity, and/or adoption of targets or goals related to board diversity (without prescribing what such targets should be, unless otherwise specified by applicable laws and regulatory requirements, or listing standards).
- Request inclusion of sexual orientation, gender identity, minority status, or protected classes, as appropriate under applicable laws and regulations, in a company's employment and diversity policies when the company has not already formally established such protections. A fund will generally not support proposals asking companies to exclude references to sexual orientation and/or gender identity, interests, or activities in their employment and diversity policies.

Oversight failures

If a situation arises in which the board has failed to effectively identify, monitor, and ensure management of material risks and business practices under its purview based on committee responsibilities, a fund will generally vote against the relevant committee chair. These risks may include material social and environmental risks.

To assess climate risk oversight failures, factors the fund will consider include:

- The materiality of the risk;
- The effectiveness of disclosures to enable the market to price the risk;
- Whether the company has disclosed business strategies, including reasonable risk mitigation plans in the context of the anticipated regulatory requirements and changes in market activity in line with the Paris Agreement or subsequent agreements; and
- Consideration for company-specific context, market regulations, and expectations.

A fund will also consider the board's overall governance and effective independent oversight of climate risk. When a specific risk does not fall under the purview of a specific board committee, a fund may vote against the chair, the lead independent director, the most senior executive director, or any relevant director(s).

Principle III: Remuneration

Remuneration policies linked to long-term relative performance are fundamental drivers of sustainable, long-term value for a company's investors. Providing effective disclosure of these practices, their alignment with company performance, and their outcomes is crucial to giving shareholders confidence in the link between incentives and rewards and the creation of long- term value. Well-designed remuneration policies help attract, retain, and motivate talented executives to drive sustainable, long-term value creation.

The funds encourage improvements in remuneration disclosure across the market and ask companies to enhance their disclosure to support effective dialogue with shareholders.

Annual retirement and bonus plans

A fund will generally vote against executive or retirement bonus-related proposals or plans where the bonus amount(s) are not disclosed.

A fund will also generally vote against plans if they are excessive or include outside directors or statutory auditors because of concerns about independence and conflicts of interest.

Equity remuneration plans

A fund will vote case by case on equity remuneration plans for employees.

In general, a fund supports companies adopting equity-based compensation plans for employees as long as the plan or plans align with long-term shareholder interests and value. When evaluating equity remuneration plans, three main factors are considered:

- Dilution to shareholders—dilution from the proposed plan and all previous plans should generally not exceed 5% for mature companies and 10% for growth companies (as long as the company provides an adequate rationale);
- Any discount on stock options;
- The company's grant history; and
- Alignment with market practice.

Director and statutory auditor fees

In general, a fund will vote for an increase in director or statutory auditor fees as long as the increase is explained and the fees seem reasonable, are in line with peers, and take into account the amount of time required to fulfill their roles.

A fund will generally vote against proposals seeking to increase director fees if there are concerns about corporate malfeasance.

Principle IV: Shareholder rights

Governance structures empower shareholders and ensure accountability of the board and management. Shareholders should be able to hold directors accountable as needed through certain governance provisions.

Annual report and accounts

Generally, a fund will vote for the annual report and accounts.

A fund may consider voting against the annual report and accounts if:

- There are concerns about the integrity of the financial statements and/or the external auditors;
- There has been a financial misstatement; and/or
- The auditor elected not to provide an audit opinion, provided a qualified audit opinion, or highlighted an emphasis of matter that was particularly concerning.

Board structure and director elections

Annual re-election of directors is considered best practice. A fund will generally vote for proposals to declassify an existing board and vote against management or shareholder proposals to create a classified board.

Additional share classes

The Vanguard funds approach to companies issuing, or proposing to issue, more than one class of stock with different classes carrying different voting rights remains philosophically aligned to "one-share, one-vote". To that end, alignment of voting and economic interests is a foundation of good governance. However, pragmatically, we remain mindful of the need not to hinder public capital formation in the equity markets. The approach supports the idea of a newly public, dual-class company adopting a sunset provision that would move the company toward a one-share, one-vote structure over time.

A fund will vote case by case on related proposals to eliminate dual-class share structures with differential voting rights and those moving toward a one-share, one-vote structure over time.

Takeover defense plans ("poison pills")

A fund will vote case by case on the introduction or renewal of a takeover defense plan.

Generally, the funds are unlikely to support a takeover defense plan when:

- The company has not provided adequate disclosure and rationale as to why the plan is required;
- The disclosure of the plan's terms and when it can be triggered are ambiguous;
- The special committee that evaluates transactions includes non-independent directors or statutory auditors;
- The overall board independence is below the thresholds set out in the Board Independence section of this policy and the Japanese Corporate Governance Code;
- The trigger threshold is below 20% of outstanding shares;
- The plan's duration is greater than three years, or a plan has been in place for more than three years in totality without adequate rationale as to why the plan continues to be renewed;
- The plan somehow undermines shareholder rights;
- The company has other mechanisms or policies that could be considered takeover defenses; and/or
- There is evidence that the plan could be abused, given past actions by the board and/or concerns about the board's oversight.

Amendments to articles of association

A fund will generally vote for minor amendments that include any administrative or housekeeping updates and corrections. When evaluating all other amendments to the articles of association, the following will be considered:

- Any changes to corporate law and/or listing rules that may require an amendment to the articles of association;
- Whether the amendments may result in corporate governance structures and/or processes that are not best practices or are a regression from what the company already does (taking into account any explanation provided by the company for the change); and/or
- Whether the amendments are detrimental to shareholder rights generally.

Reincorporation/change of domicile

A fund will vote case by case on proposals to reincorporate to another country and/or proposals for companies to change their primary listing.

A fund will consider the reasons for the relocation, including the company's history, strategy, and shareholder base along with any differences in regulation, governance, and shareholder rights.

Shareholder proposals

A fund will vote case by case on all shareholder proposals, taking into account the requests of the proposal, the level of prescription, the supporting rationale from the proponent and the company's response, and whether the board has already adequately addressed the issue or taken steps to address the issue outlined in the proposal.

Shareholder meeting rules and procedures

- *Quorum requirements.* A fund will generally vote against proposals that would decrease quorum requirements for shareholder meetings below a majority of the shares outstanding, unless there are compelling arguments to support such a decrease.
- *Approve "other such matters that may come before the meeting" or "any other business."* A fund will generally vote against a proposal to approve "other such matters that may come before the meeting."
- *Approve deliberations on possible legal action against directors if presented by shareholders.* A fund will generally vote against such a proposal because of the lack of disclosure regarding the proposed deliberation.
- *Adjourn meeting to solicit more votes.* In general, a fund will vote for the adjournment if the fund supports the proposal in question and against the adjournment if the fund does not support the proposal.
- *Bundled proposals.* A fund will vote case by case on all bundled management proposals.
- *Change of date, time, or location of annual general meeting.* A fund will typically vote for management proposals to change the date, time, or location of the annual meeting if the proposed changes are reasonable.
- *Virtual meetings.* A fund will generally support proposals seeking to conduct "hybrid" meetings (in which shareholders can attend a physical meeting of the company in person or elect to participate online). A fund may vote for proposals to conduct "virtual-only" meetings (held entirely through online participation with no corresponding physical meeting taking place). Virtual meetings should not curtail shareholder rights, for example by limiting the ability for shareholders to ask questions. A fund will generally support if:
  - Meeting procedures and requirements are disclosed ahead of a meeting;
  - A formal process is in place to allow shareholders to submit questions to the board;
  - Real-time video is available and attendees can call into the meeting or send a prerecorded message;
  - Shareholder rights are not unreasonably curtailed; and/or
  - Applicable laws and regulations provide relevant safeguards to shareholder rights, and the company complies with these provisions.

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