

Roundtable Discussion between Outside Audit & Supervisory Board Members (Independent)

Deepening Diversity and Strengthening Growth Potential
Contributions to Corporate Value by Outside Audit & Supervisory Board Members

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Role and Posture of Outside Audit & Supervisory Board Members (Independent) to Meet the Expectations of Stakeholders

Uchiyama: Under the Companies Act of Japan, the role of company auditors is to audit the execution of duties by directors. Having been elected at the General Meeting of Shareholders of OMRON, we audit the execution of duties by Directors in order to earn the trust of stakeholders. At the same time, however, OMRON wants both Directors and Audit & Supervisory Board Members to serve as one team in performing their functions to enhance corporate value, while always mindful of their respective legal statuses. OMRON's Corporate Governance Committee consists of Outside Directors and Outside Audit & Supervisory Board Members and its main function is to evaluate and report on the effectiveness of the Board of Directors. However, going beyond evaluating and reporting on effectiveness, this committee serves as a forum for those being supervised and those supervising to exchange frank opinions on how to improve governance. Furthermore, in the process of deliberating on the formulation of the long-term vision "SF2030" and

the medium-term management plan "SF 1st Stage," we, Outside Audit & Supervisory Board Members, actively participated in the discussions at the Board of Directors meetings to ensure more effective monitoring.

Kunihiro: Yes, that's right. I think Audit & Supervisory Board Members should actively participate in discussions at meetings of the Board of Directors in their capacity as board members. Some companies consider the role of auditors is to check the directors' discussions when necessary and otherwise to keep quiet. But OMRON does not see it that way. At OMRON, three Outside Directors and two Outside Audit & Supervisory Board Members with great experience in wide-ranging fields represent stakeholders and discuss OMRON's potential and how to enhance its corporate value. In doing so, we are not preoccupied with whether we are Audit & Supervisory Board Members or Directors. Of course, when it is necessary to prevent damage to corporate value, Audit & Supervisory Board Members must apply the brakes to fulfill their role. That is ultimately the point of being Audit & Supervisory Board Members. However, such situations are rare. We, Outside Audit & Supervisory Board Members, will consider various

aspects of OMRON's corporate value from outside perspectives in response to the views expressed by internal parties. For this purpose, there is no distinction between Outside Directors and Outside Audit & Supervisory Board Members.

Uchiyama: What we must always keep in mind is that we are representing stakeholders, as Mr. Kunihiro just mentioned. We must consider what we should do to enhance or prevent damage to OMRON's corporate value from the viewpoint of "representatives of stakeholders."

Kunihiro: According to the traditional view, there are "offensive" discussions to enhance corporate value and "defensive" discussions to prevent damage to corporate value, and both of internal and outside Audit & Supervisory Board Members, should focus exclusively on "defensive" discussions and not get involved in "offensive" discussions. However, defense and offense cannot be neatly separated in that way. Since we are living in uncertain times and prospects are unclear, risk management is inextricably linked to finding opportunities. So, the roles cannot be neatly separated. To maintain that Outside Directors should be "offensive" and Outside Audit & Supervisory Board Members should be "defensive" is simplistic. For example, Outside Directors should be involved in discussions on compliance and Outside Audit & Supervisory Board Members should be involved in discussions on growth strategies.

Therefore, Outside Executives need to be eagle-eyed, knowledgeable, and insightful concerning the company. For example, "I am an Audit & Supervisory Board Member, so I don't know anything about growth strategies," would not be a helpful attitude. It is also important that diverse Outside Directors and Outside Audit & Supervisory Board Members can communicate fully with one another and work constructively together while demonstrating their personal qualities.

Evaluation of Long-term Vision and Medium-term Management Plan and OMRON's Issues from Outside Perspectives

Uchiyama: A project team consisting of people from whom the next generation of OMRON's leaders will likely be selected identified the fields where OMRON should compete, based on their view of current circumstances and forecasts of the changes shaping the future business environment presented by the executive team. This is how the long-term vision "SF2030" and the medium-term management plan "SF 1st Stage" were formulated with a timeframe extending far into the future. I highly regard the fact that the members involved in the project took the initiative, assumed responsibility, and developed the narrative of OMRON's enhancement of corporate value in an objective manner.

OMRON's management, based on the SINIC Theory proposed by OMRON founder Kazuma Tateishi accords value to predicting the future based on an appreciation that three elements, namely, science, technology, and society, develop cyclically. In addition to these three elements, I think the new long-term vision has another element, the global environment. However, in the global market where OMRON operates, the stages of social development such as "introduction of IT" and "optimization," are discontinuous and unbalanced. In addition, I believe that the cycle has been accelerating owing to the progress of digital technology. In other words, no matter how elaborate a vision or plan may be, there is always a risk that unpredictable environmental changes will occur that render the vision or plan obsolete. So we must recognize such environmental changes and act accordingly. Or, even in times when it is particularly difficult to predict the future, if you can create the future through innovation, there will be no need for prediction. With regard to such autonomous initiatives, I have great expectations of OMRON.

Kunihiro: Management issues related to achieving this long-term vision and the medium-term management plan will be the themes that we Outside Audit & Supervisory Board Members will monitor from now on.

Uchiyama: Absolutely. As I mentioned, I highly regard OMRON's plan for SF2030, but on the other hand I have some concerns. For example, when we interview the managers responsible for OMRON's businesses, they give polished presentations and respond to our questions well. I wonder whether there are signs of "big company disease." I say this because, in order to achieve the vision, it is important to be ready and willing to implement a plan even if there is a 30% risk provided there is a 70% chance of success, as Kazuma Tateishi advocated in his "7:3 Principle" regarding the venture spirit. It is also important to resolve on-site issues promptly. I feel that too polished a presentation might be an indication that OMRON managers may be succumbing to the mindset of seeking "10:0" instead of "7:3."

So, I have recently changed the nature of my questions. I ask OMRON managers: "What are three issues that you have as the person in charge of this business?" In order to fulfill my responsibility as an Outside Audit & Supervisory Board Member, I need to bring inherent management issues to the surface and focus on whether OMRON is implementing effective measures to deal with them. I would like those responsible for OMRON's businesses to appreciate this.

Kunihiro: I totally agree with you. It is natural that there will be difficulties and challenges to overcome, and I hope OMRON managers will be shrewd enough to use Outside Executives to address these challenges. We, Outside Audit & Supervisory Board Members, as well as Outside Directors, share a concern that OMRON's venture



spirit may be weakening. In plain words, “boldness” may be weakening. OMRON is a very well-organized company with solid management based on a corporate philosophy, but I feel that the OMRON Principles based on the founder’s venture spirit are sometimes put in a “frame” and hung on the wall and are not really a springboard to decisive action by OMRON.

Tackling challenges and innovating to advance boldly are not at odds with management based on a corporate philosophy, rather they can be integral to it. But I cannot deny my impression that OMRON feels comfortable when chanting its corporate philosophy by rote and sometimes doesn’t translate it into action.

As an indication of this concern, investors have commented that the challenge for OMRON is to have an insatiable appetite for progress. We are aware of that.

Uchiyama: Looking at the figures regarding OMRON’s growth potential, total assets increased 73% from ¥537.3 billion in fiscal 2011, 10 years ago, to ¥930.6 billion in fiscal 2021, while the number of employees decreased from 35,992 to 29,020 in 10 years, and capital efficiency has also improved. However, when it comes to sales, OMRON’s net sales have grown only 23% over the 10 years from ¥619.5 billion in fiscal 2011 to ¥762.9 billion in fiscal 2021. Some companies in the same industry as OMRON have nearly quadrupled their sales over the past decade. That is why OMRON’s lack of growth is pointed out.

OMRON uses return on invested capital (ROIC) as a KPI in management, but ROIC is an efficiency indicator and does not include the concept of growth. There is a need to examine whether the emphasis on ROIC has been at the expense of growth.

I agree with Mr. Kunihiro about management based on corporate philosophy. The OMRON Principles should be the driving force behind OMRON’s focus on identifying social needs and its wholehearted pursuit of solutions. You can only say that the corporate philosophy has penetrated when management based on the corporate philosophy has reached that level.

Kunihiro: The key to strengthening OMRON’s growth potential is to take advantage of its diversity. The actions of all OMRON employees are based on the OMRON Principles. This is the result of management based on the corporate philosophy and it is one of OMRON’s strengths. But at the same time, we are concerned that the OMRON Principles might become a superficial phenomenon rather than penetrating and that OMRON employees might become increasingly homogeneous.

The investment in JMDC Inc. in February 2022 was the subject of much discussion at the Board of Directors meeting, as it was a case of investment in a company with a very different corporate culture. OMRON Directors and Audit & Supervisory Board Members agreed that the investment in JMDC should be a catalyst for changing OMRON by learning from JMDC’s corporate culture, rather than trying to instill OMRON’s corporate culture and ways of doing things in JMDC. In pursuing collaboration and synergy, if OMRON were to attempt to compel the partner to become like OMRON, the partner’s momentum would cease and collaboration would go nowhere. OMRON should emulate those attributes of the partner in which OMRON is deficient while maintaining a healthy tension and distance.

Evaluation of Effectiveness of the Audit & Supervisory Board and Issues to be Addressed

Uchiyama: Every year, OMRON conducts a questionnaire-based evaluation of the effectiveness of the Audit & Supervisory Board, and along with self-evaluation, issues for the next fiscal year are identified. This year, three issues were identified: (1) enhancing opportunities for more open discussion between Audit & Supervisory Board Members and Outside Directors, (2) considering a new approach for auditing in an increasingly uncertain business environment and reforming the Audit & Supervisory Board, and (3) strengthening cooperation with the Internal Audit Division to further enhance its performance.

As I mentioned at the outset, I believe that both Directors and Audit & Supervisory Board Members should fulfill their functions to enhance corporate value as one team while taking into account their respective stances. We have long been making efforts to break down the barriers between Outside Directors and Outside Audit & Supervisory Board Members. However, the Corporate Governance Committee is the only committee of which Outside Audit & Supervisory Board Members are a part of. As the Corporate Governance Committee is a voluntary committee that does not meet frequently, there are not many opportunities for Outside Directors and Outside Audit & Supervisory Board Members to discuss their views in a formal setting.

Kunihiro: That is why we have been creating opportunities for the five Outside Executives (Outside Directors and Outside Audit & Supervisory Board Members) of OMRON to meet and discuss on an ad hoc basis, in addition to discussion in a formal setting as in a committee meeting. The role of both Outside Directors and Outside Audit & Supervisory Board Members is to oversee execution as representatives of stakeholders, always with a view to accomplishing the goal of enhancing corporate value. Therefore, it is in the best interest of OMRON to have Outside Directors and Outside Audit & Supervisory Board Members discuss freely and openly and collaborate as one team, rather than remaining in silos corresponding to the difference in their legal statuses under the Companies Act.

Uchiyama: “Enhancing opportunities for more open discussion” does not mean simply increasing the number of discussions but rather to always act based on that awareness. So, from now on, this mindset will be important.

Kunihiro: That’s right. The mindset of Outside Executives will be tested in the future. Outside Directors and Outside Audit & Supervisory Board Members should be predisposed to act for the purpose of enhancing corporate value and preventing damage to corporate value, rather than simply following what is stipulated in the Companies Act or the Corporate Governance Code about the roles of outside directors and outside company auditors.

In this era of change, risks and opportunities are shrouded in fog and always in flux. In these circumstances, it would be wasteful to segregate outside directors from outside company auditors who, by virtue of their wide-ranging backgrounds, have much to offer. It would prevent them from making a valuable contribution to the management of OMRON. At Japanese companies, outside auditors’ narrow conception of their own role and a sense of corporate stagnation may be connected. The second issue, “considering a new approach for auditing in an increasingly uncertain business environment and reforming the Audit & Supervisory Board,” concerns the operation of auditing. OMRON’s Audit & Supervisory Board has been quite progressive compared to counterparts at other companies, but we are looking for ways to improve the operation of auditing.

Uchiyama: We are considering that the activities of the Audit & Supervisory Board in various phases should be evaluated objectively.

Kunihiro: Is the Audit & Supervisory Board really useful? In what sense are these activities of the Audit & Supervisory Board meaningful? Such questions have a particular resonance for us as Outside Audit & Supervisory Board Members, and our evaluation by the Board of Directors and other bodies, for example, would be valuable, leading to improvements.

Uchiyama: Regarding the third issue, “strengthening cooperation with the Internal Audit

Division,” I would like to express my opinion. The conventional auditing by OMRON’s Internal Audit Division is, to put it simply, to check whether compliance is ensured. I would like this to be changed. I want the Internal Audit Division to perform internal auditing from the perspective of Audit & Supervisory Board Members and enhance risk-management-oriented internal audit functions. For this purpose, strengthening cooperation between the Audit & Supervisory Board and the Internal Audit Division is necessary.

For example, when you audit a subsidiary and find a problem, what is the recognition of the person in charge of the subsidiary about management issues, how are these issues addressed, are measures adequately implemented, and is the relationship with the parent company properly taken care of? We are telling the Internal Audit Division that they need to adopt such perspectives, otherwise they will not know where the risks are.

Kunihiro: Internal audits progress from audits to find deficiencies to risk-based audits, and then to management audits. If the concept of risk management as broadly conceived, policies, and strategies do not permeate workplaces, they will not benefit the company. The Internal Audit Division must be able to find out what is really happening. The consensus among us is that whether a company’s growth strategy is actually working should also be subject to audit. The Internal Audit Division cannot adopt such an approach in a single step, but the Audit & Supervisory Board will encourage and cooperate with the Internal Audit Division to move in that direction.

Uchiyama: In doing business globally with overseas sales accounting for 60% of total net sales, it is essential for OMRON to grasp what is happening at each site and to constantly examine, improve, and refine its basic functions, such as development, production, and sales, as well as its management decision-making process to draw out the potential of the diverse human resources underpinning the OMRON Group. I believe this is a precondition for securing OMRON’s future growth.

