

## ■ Message from the Chairman of the Board

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# Effective Governance to Win Among Global Competition

Creating and maintaining an appropriate system of governance is key to sustaining and maximizing the growth of shareholder value over the short, medium and long term. I believe that optimal corporate governance entails the creation of an environment in which all discussions and decision-making processes related to management policy and business strategy are designed to contribute to shareholder value. Moreover, the implementation of such policy and strategy should be monitored to provide feedback and feed-forward. Of course, it goes without saying that governance systems must also ensure compliance with the laws of relevant countries as well as globally acceptable standards of fairness and transparency.

In line with this basic approach, Tokyo Electron's Board of Directors is composed of three types of directors, namely outside directors, non-executive directors and executive directors. In addition, Tokyo Electron has an Audit & Supervisory Board, which audits the appropriateness and fairness of the executive directors' decision-making processes and business execution, as well as the auditing methods and results of the independent auditors. The Audit & Supervisory Board currently has five members, three of whom are outside members. The composition of the Board of Directors enables aggressive management—allowing appropriate risk taking in order to increase corporate value—as well as effective defensive governance by monitoring the risks being taken.

Tokyo Electron has also voluntarily established a Nomination Committee and Compensation Committee within the Board of Directors. The guidelines and policies that guide the activities of these committees are thoroughly discussed by the Board of Directors. Furthermore, in fiscal 2017, we further enhanced our existing succession program to groom candidates for the CEO and other top management positions.

Over the past few years, many Japanese companies have adopted measures to comply with the Corporate Governance Code. This has propelled governance in the country as a whole to a new level of thoroughness. Globally, however, we are seeing continued efforts to make governance even stronger, such as stepping up board diversity or bolstering the number of outside directors and effective use of their perspectives. For Tokyo Electron to sustainably grow in the semiconductor and electronics industries, it is extremely important to pursue diversity among both internal and external directors while also ensuring the selection of directors who are best equipped to contribute to corporate growth and shareholder value. As chairman of the board, I will continue working to ensure that Tokyo Electron's governance system helps increase shareholder value and that the Board of Directors operates effectively.



**Tetsuo Tsuneishi**  
Chairman of the Board



■ Corporate Governance

Corporate Governance

Basic stance

In an environment where over 80% of our sales come from overseas, Tokyo Electron regards maintaining governance as essential to becoming a truly global company that achieves sustainable growth.

To that end, Tokyo Electron strives to build frameworks to maximize the use of its worldwide resources. In addition to strengthening its management platform and technology base, the Company maintains a governance structure that will enable it to attain world-class profitability.

Tokyo Electron uses the Audit & Supervisory Board System, which consists of a Board of Directors and an Audit & Supervisory Board. Effective governance is achieved based on the supervision of management by the Audit & Supervisory Board.

Board of Directors

1. Roles and responsibilities of the Board of Directors

The Board of Directors works to achieve sustainable growth and increase corporate value over the medium to long term based on its fiduciary responsibility to shareholders. The roles and responsibilities of the Board of Directors are as follows:

- (1) Establishing management strategy and vision
- (2) Making major operational decisions based on strategic direction
- (3) Engaging in constructive, open-minded debate

The Board of Directors seeks the active participation of those present in discussions in order to obtain a wide range of opinions, and supervises management and operational execution based on active debate.

The Board of Directors respects minority or opposing viewpoints, including opinions voiced by outside directors; revises the conditions for implementation or the content of proposals as necessary; and engages in extensive debate with the goal of reaching decisions based on consensus. However, emphasis is placed on making necessary decisions quickly to avoid missing opportunities.

2. Board size and independent outside directors

Tokyo Electron considers it essential to maintain a Board of Directors with the appropriate size to ensure high quality, active debate and the diversity expected of both executive directors and independent directors. The current Board of Directors consists of 12 directors, and Tokyo Electron believes this to be the appropriate size, at present, to achieve a good balance in terms of knowledge, experience and skills.

Tokyo Electron regards the active expression of opinions, not only by independent directors, but also by Audit & Supervisory Board Members, as the cornerstone that supports the sound decision making of the Board of Directors. Currently, five out of the 17 participants in the Board of Directors meetings, including the Audit & Supervisory Board Members, are outside members, consisting of two independent directors and three outside Audit & Supervisory Board

Members. Tokyo Electron believes that the current Board of Directors meetings achieve an appropriate sense of productive tension and constructive debate due to the combined presence of executive directors, essential for making operational decisions, and outside members, who provide objectivity.

3. Nominations for Director and CEO

Tokyo Electron has established a Nomination Committee to ensure fairness and efficiency in management. The Nomination Committee proposes director candidates to the Board of Directors prior to their election at the General Meeting of Shareholders and also nominates CEO candidates for appointment by the Board of Directors. The CEO is not part of the Nomination Committee, and the authority to propose the election or dismissal of the CEO or directors is entrusted to the Nomination Committee.

4. Director and CEO compensation

Aiming to strengthen its global competitiveness and increase management transparency, Tokyo Electron has adopted a director and executive officer compensation system that is closely linked to performance and shareholder value. The compensation of directors and executive officers comprises a fixed monthly wage and an annual performance-linked bonus.

The Compensation Committee, which comprises three or more directors and includes at least one outside director, conducts an analysis of industry wage levels in and outside Japan, accounting for both monetary and non-monetary aspects of the total compensation package. Based on this comprehensive analysis, the committee proposes a policy and system for the compensation of the Board of Directors and executive officers as well as individual compensation amounts, including bonuses, for the CEO and the representative directors.

In order to better link factors that increase corporate value and shareholder value to compensation, Tokyo Electron has designated the net income attributable to owners of the parent and return on equity (ROE) for the current period as the main calculation benchmarks in the performance-linked compensation system for the CEO and other directors. These are adjusted, as necessary, for extraordinary income/losses and other special factors.

In principle, performance-linked compensation consists of monetary compensation and share-based compensation; the ratio of these two components is roughly 1:1 for directors, and single year performance is appropriately reflected in the performance-linked compensation of the CEO and other directors. Share-based compensation is awarded in the form of stock options with the exercise price set at one yen per share, and a three-year vesting period from the date of allotment before the options may be exercised.

5. Evaluation of the effectiveness of the Board of Directors

Each year, based on an evaluation survey filled out by the Board of Directors and Audit & Supervisory Board Members, the Board of the Directors analyzes and evaluates its own effectiveness through discussions, mainly involving the outside directors and outside Audit & Supervisory Board Members, as well as separate discussions involving the entire Board of Directors. The board then discloses a summary of the results.

Tokyo Electron's Board of Directors receives regular reports from the CEO and other executive directors and designates issues for discussion at each board meeting. The directors and Audit & Supervisory Board Members actively discuss these reports and issues based on their diverse viewpoints and experiences. Meeting participants exchange opinions in an open, unrestrained manner and engage in real debate. As a benefit of this thorough discussion, proposals made by executive members may subsequently be amended to reflect the opinions of outside directors and Audit & Supervisory Board Members prior to passage. Tokyo Electron thus believes that its Board of Directors is able to carry out its role appropriately and function effectively.

Based on the insights gleaned from the most recent evaluation, Tokyo Electron is working to make the Board of Directors even more effective. Priorities include expanding time allotted for the discussion of issues related to Group policy and strategy, including major management issues and medium- to long-term management and growth strategies, as well as enhancing opportunities for dialog with the outside directors and outside Audit & Supervisory Board Members. Furthermore, the Board of Directors will continue to discuss and examine its own operation and composition, including questions of diversity.

Does Tokyo Electron have these major components of corporate governance?

Compensation Committee	Yes	Composed of directors, including outside directors and excluding representative directors, or Audit & Supervisory Board Members
Nomination Committee	Yes	Composed of directors, excluding the CEO, or Audit & Supervisory Board Members
Outside directors	Yes	Two of the 12 directors are outside directors
Outside Audit & Supervisory Board Members	Yes	Three of the five Audit & Supervisory Board Members are outside Audit & Supervisory Board Members
Executive officer system	Yes	
Disclosure of individual remuneration of representative directors	Yes	Disclosed since 1999
Performance-linked compensation system	Yes	
Stock options system	Yes	Does not apply to outside directors and Audit & Supervisory Board Members
Retirement allowance system for executives	No	
Anti-takeover measures	No	

## ■ Messages from the Outside Directors

## Messages from the Outside Directors



Outside Director  
Hiroshi Inoue

Currently serving as honorary chairman and director and previously as chairman of Tokyo Broadcasting System Holdings, Inc., Mr. Inoue possesses a wealth of experience and insight in corporate management.



Outside Director  
Charles Ditmars Lake II

Serving as chairman and representative in Japan of American Family Life Assurance Company of Columbus, and also as president of Aflac International, Incorporated, Mr. Lake has a great deal of experience and knowledge in corporate management bridging Japan and the United States.

Tokyo Electron should be very proud of its excellent performance in fiscal 2017.

The semiconductor production equipment industry is subject to major market ups and downs. I greatly admire the work of President Kawai, the rest of Company's executives and its employees, which has successfully secured a solid foothold for Tokyo Electron in this volatile environment.

These achievements are, I think, the fruit of the united efforts of the entire Company since the merger with Applied Materials was called off two years ago. At the same time, it is clear to me that the foundation for these results is the outstanding technological prowess and relationships of trust with customers that Tokyo Electron has built up since its founding.

As the internet of things (IoT) expands, the semiconductor industry is undergoing major structural change, making it very difficult to predict demand. To continue to thrive in this market, I believe Tokyo Electron will have to achieve qualitative change in how it interacts with customers. The foundation underpinning this, however, is still the ongoing reinforcement of Tokyo Electron's technological superiority and excellent reputation. I am confident that, through the steady application of such efforts, Tokyo Electron will ultimately increase its corporate value and remain a leader in the semiconductor industry as the industry continues to expand.

I look forward to seeing where Tokyo Electron is going next, and I will do my utmost to help it get there.

Heightened economic uncertainty has led to an increasingly challenging global business environment amid factors including geopolitical turmoil, critical elections in Europe, and the anti-globalist challenge to the Bretton Woods system. Against this backdrop, and as stakeholder expectations continue to evolve, this is an era in which robust corporate governance is more critical than ever for global businesses to continue to achieve sustainable growth.

Tokyo Electron was an early adopter of corporate governance systems consistent with global best practices. Indeed, as Japan moves toward a major turning point in its corporate governance environment, Tokyo Electron has continued to set an example, earning it a strong reputation among market participants.

Last year, I began my role as an independent outside director, wanting to play a part, however small, in further enhancing Tokyo Electron's corporate value. Since then, both in and out of Board meetings,

I have been engaged in active and meaningful discussions with internal directors, Audit & Supervisory Board Members, and outside directors on important business matters related to medium- to long-term human capital development and exploring initiatives to take corporate governance systems to the next level. In order to fulfill my duties as an independent outside director, based on Tokyo Electron's basic policy, I will strive to proactively raise issues from an objective and professional standpoint. Looking back on the activities of the past year, I am convinced that Tokyo Electron's corporate governance system is substantially effective in both form and function.

In fulfilling my duties as an independent outside director, I will continue working to contribute to the development of an even stronger corporate governance system, underpinning a new start for Tokyo Electron to become a truly global company.

Messages from the Outside Audit & Supervisory Board Members

Messages from the Outside Audit & Supervisory Board Members

Audit & Supervisory Board

The Audit & Supervisory Board currently consists of five members and includes three outside Audit & Supervisory Board Members. Two members are full-time. The full-time Audit & Supervisory Board Members collect information through onsite surveys, and the board maintains appropriate coordination with the Internal Audit Department and the independent auditors as part of a structure that enables Audit & Supervisory Board Members to obtain all information necessary for audits.

Moreover, the composition of Audit & Supervisory Board Members provides a good balance of knowledge required for operational audits and accounting audits, including financial and accounting knowledge, legal knowledge, and audit experience at other companies. Tokyo Electron thus believes its Audit & Supervisory Board Members are able to perform their auditing functions effectively.

Internal Control System and Risk Management

Basic Stance

In order to enhance the Tokyo Electron Group's corporate value and remain accountable for our actions to our stakeholders, we are making efforts to strengthen effective internal control. This involves implementing practical measures that are in line with the Fundamental Policies concerning

Internal Controls within the Tokyo Electron Group, set out by Tokyo Electron's Board of Directors. We are also annually evaluating our internal control over financial reporting based on the Financial Instruments and Exchange Act of Japan.

Risk Management System

To more effectively strengthen the internal control and risk management systems of the entire Group, Tokyo Electron has established a dedicated risk management and internal control function within the General Affairs Department of the corporate headquarters. This function analyzes the risks faced by the Group and identifies material risks. It then monitors the management of such risks while supporting and implementing risk management activities. The function also regularly reports the status of risk management activities to the Audit & Supervisory Board Members and the Board of Directors.

In fiscal 2017, the Group reassessed the material risks in its operating environment. For each risk determined to be material, the status of risk management at the responsible divisions was reconfirmed. Going forward, the Group will continue these initiatives to enhance the efficacy of its risk management framework.

Auditing by the Internal Audit Department

The Global Audit Center of the corporate headquarters is the Group's internal audit department. This Center is

responsible for auditing business activities, compliance and systems at domestic and overseas Group companies and business units (BUs) in accordance with each fiscal year's auditing plan. The Center also annually evaluates the effectiveness of the Group's internal control over financial reporting based on the Financial Instruments and Exchange Act of Japan.

At operating divisions where issues have been identified through audits and assessments, the Center monitors progress and provides necessary guidance for improvement.

Business Continuity Plans (BCPs)

The Tokyo Electron Group began building business continuity plans in 2003. After the Great East Japan Earthquake, the Group rebuilt these plans to be more effective and include provisions for restoring operations after crises, focusing on major business sites. As examples of specific initiatives, the Group has put considerable effort into such preparations for disasters as stockpiling emergency supplies (including food and drinking water), reinforcing essential infrastructure, rebuilding the safety confirmation system, creating manuals, and implementing drills and employee training.

Message from the Outside Audit & Supervisory Board Member

Outside Audit & Supervisory Board Member  
Takatoshi Yamamoto

Mr. Yamamoto has extensive experience as a securities analyst covering the electronics industry as well as expert knowledge of global finance and accounting. He is concurrently serving as an outside director at Hitachi, Ltd.



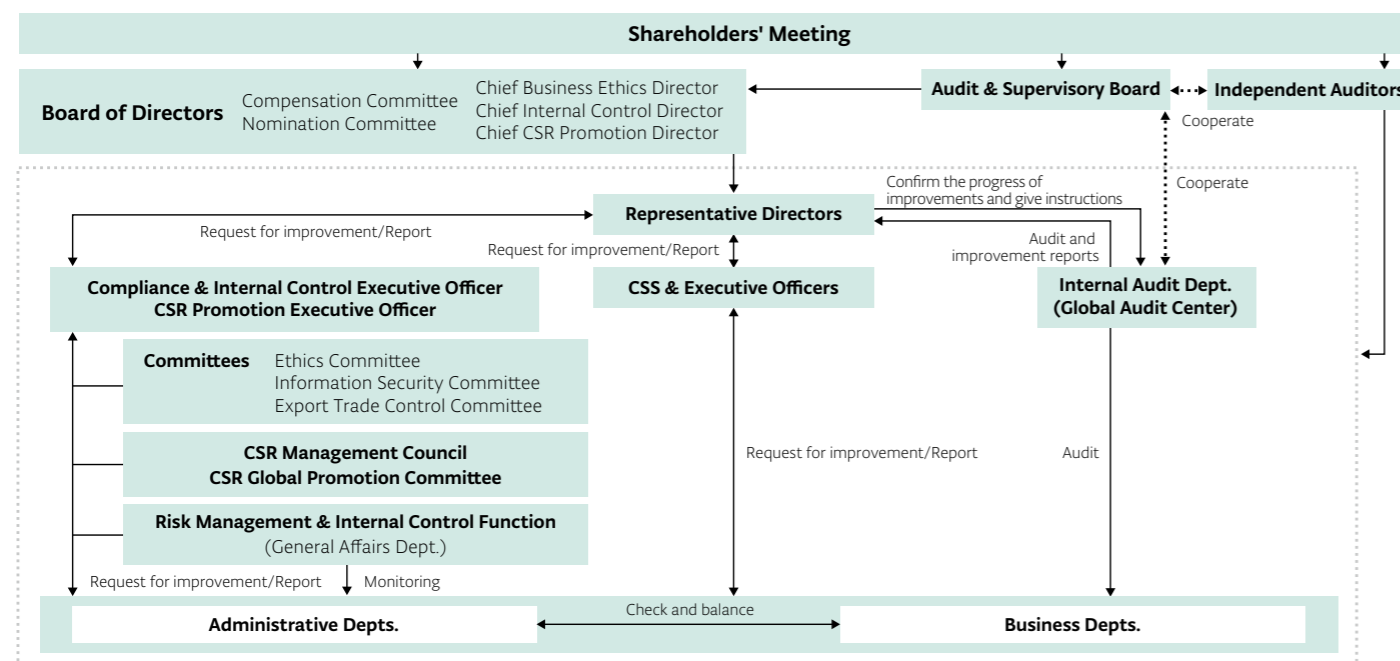
I have now served as an outside Audit & Supervisory Board Member for four years, beginning in 2013. The initial two year period was marked by work toward the planned merger with Applied Materials. The next two years, after the merger was called off, have been focused on charting a new course for Tokyo Electron. During these four years, the importance of strengthening corporate governance has been the subject of much discussion across Japan, including questions related to earnings power, the sustained improvement of corporate value and effective institutional design. These crucial issues have also received careful consideration at Tokyo Electron as the Company marked a new beginning, aiming to maintain a healthy sense of urgency while evolving into a truly global company that boasts world-class profitability.

Tokyo Electron has been able to do this thanks to its highly effective Board of Directors. The board has vigorously debated subjects including lessons learned from the merger process, technological innovation in semiconductor production, the development of new technologies and products, operational

efficiency, the numerical targets of the medium-term management plan, and new measures to return profits in order to raise shareholder value. The board continues to strive to reflect these discussions in business execution and ensure the effective oversight and monitoring of the resulting developments.

As global business prospects expand, opportunities to grow Tokyo Electron's profitability and corporate value to world-class levels through the effective combination of such aggressive management and careful oversight are emerging. As an outside Audit & Supervisory Board Member, I will strive to remain highly alert, diligently analyzing risks in and outside the Group from an objective standpoint. I will work to increase the overall effectiveness of audits through a three-pronged approach, in conjunction with the Internal Audit Department and accounting auditors, and provide oversight and monitoring to ensure proper corporate behavior. I believe that doing these things is the key to meeting the expectations of shareholders and other stakeholders.

Corporate Governance Framework, Internal Control System and Risk Management System



## ■ Messages from the Outside Audit &amp; Supervisory Board Members

**Messages from the Outside Audit & Supervisory Board Members**

Furthermore, to meet its responsibilities as an equipment manufacturer, the Group pursues ongoing efforts to improve its BCPs, including taking steps to facilitate early recovery and alternate production.

When the Kumamoto Earthquake struck in April 2016, the Group was able to respond with speed and precision based on the BCP it had prepared.

**Information Security Management**

To ensure the appropriate management of information assets, the Group has an information management framework centered on its Information Security Committee, which is composed of representatives from departments across the Group.

The Information Security Committee acts as a decision-making body for the Group. Rules concerning the handling and protection of such sensitive information as trade secrets and personal information are formulated based on the committee's policy and applied throughout the Group. An e-learning system is used to educate and promote awareness of these rules among Group employees and executives.

Additionally, the Group has a reporting system for both actual and potential cases (incidents) of information leakage. Reported incidents are quickly settled and then analyzed. Based on such analyses, recurrence prevention measures are implemented throughout the Group.

In order to mitigate emerging cyber security threats, the Group examines and undertakes rational countermeasures as necessary. The Group also has in place systems to detect targeted threats that utilize social engineering as well as a supervisory framework to prevent damage.

**Business Ethics and Compliance****Basic Stance**

Stakeholder trust is the cornerstone of business activities. In order to maintain trust, it is necessary to continuously act in rigorous conformity to business ethics and compliance. In line with the Fundamental Policies concerning Internal Controls within the Tokyo Electron Group, all Group executives and employees are required to maintain high standards of ethics and to act with a clear awareness of compliance.

**Business Ethics**

In 1998, Tokyo Electron formulated the Code of Ethics of the Tokyo Electron Group as a set of uniform standards to govern

all of its global business activities. In the same year, the Company appointed a Chief Business Ethics Director and established the Ethics Committee, which is responsible for promoting business ethics awareness throughout the Tokyo Electron Group. The Ethics Committee comprises the Chief Business Ethics Director, the Ethics Committee Chairman, and presidents of major Group companies in and outside Japan. The members meet semiannually, report on ethics-related issues facing each company, and discuss measures to further improve ethical behavior and compliance.

The Code of Ethics is reviewed in response to changes in the expectations of society. In January 2015, an anti-corruption statement was added to its introduction based on Principle 10 of the UN Global Compact, which concerns working against corruption including extortion and bribery. In August 2016, the Group revised the Code of Ethics in light of the Code of Conduct of the EICC®\* and broader social changes.

The Tokyo Electron Group's Code of Ethics and its Q&A section are published in Japanese, English, Korean and Chinese and disclosed on the intranet to enable all Group executives and employees, including those overseas, to view them at any time. The Code of Ethics is also publicly accessible from the corporate website.

<http://www.tel.com/ir/policy/compliance/ethical.htm>

\* EICC is a registered trademark of Electronic Industry Citizenship Coalition Incorporated.

**Compliance System**

Tokyo Electron has appointed a Compliance & Internal Control Executive Officer from among its executive officers to raise awareness of compliance across the Group and further improve Group-wide compliance. Each Group company has also drawn up its own compliance regulations, setting out basic compliance-related requirements in line with the Code of Ethics. The compliance regulations are intended to ensure that all individuals who take part in the business activities of the Tokyo Electron Group clearly understand the pertinent laws and regulations, international standards and internal company rules, and consistently apply these rules in all of their activities.

**Compliance Education**

Through the Group's e-learning system, we provide web-based training programs covering the basics of compliance, export-related compliance, protection of personal information, the Act for Subcontracting and other topics. All executives and

employees are required to complete these programs. In addition, other web-based programs tailored to specific positions and job roles are also available, including those on insider trading and the Social Security and Tax Number System.

We also have a quiz-based business ethics and compliance education course, launched in fiscal 2014, for all Group executives and employees. Updated yearly, the quiz is intended to maintain compliance awareness throughout the Group and disseminate the latest information.

In addition to these web-based courses, we organized in-house seminars in fiscal 2017 for Corporate Directors and executive officers on the subjects of compliance and internal control.

**Internal Reporting System**

The Tokyo Electron Group has an internal reporting system that employees can use to report any activity suspected of being in breach of laws, regulations or business ethics. An ethics hotline and a compliance hotline have been established to receive reports from all Group companies, and each overseas location also has its own reporting system. In all instances, the system ensures that whistleblowers remain anonymous and are protected from any disadvantage or repercussions.

There were no reports or cases of non-compliance with laws, regulations, or principles of ethics in fiscal 2017 that could have had a material impact on the Group's business or local communities.

**Message from  
the Outside Audit &  
Supervisory Board Member****Outside Audit & Supervisory Board Member****Ryuji Sakai**

Serving as a partner at Nagashima Ohno & Tsunematsu, Mr. Sakai possesses abundant experience and expert knowledge as an attorney at law specializing in the Companies Act, M&A, and international transactions.



One of Tokyo Electron's defining strengths is the way the Company brings together insights derived from front-line experience to drive business development, unleashing the maximum benefits of long-standing Japanese manufacturing practices. Tokyo Electron is deeply committed to the semiconductor industry. With the arrival of the internet of things (IoT), this industry has been undergoing dramatic development. Going forward, within this industry, the role that Tokyo Electron plays—as well as the business opportunities available to it—will only grow.

Given this environment, to meet shareholder expectations by continuously expanding corporate value, Tokyo Electron must make full use of its strengths as a representative of Japanese manufacturing with an outstanding customer reputation.

At the same time, management must be willing to take bold risks when necessary. It is also extremely important to proactively work to meet the expectations that exist for a global company such as Tokyo Electron, including further enhancing compliance frameworks and employee diversity.

Fortunately, Tokyo Electron's leadership is comprised of ambitious, flexibly thinking individuals. The Board of Directors freely engages in open and vigorous discussion, and the Company is set up to facilitate the aggressive management decision making necessary for growth. I will continue to carry out my duties as an Audit & Supervisory Board Member, particularly in the area of defensive governance. By doing so, I hope to contribute to Tokyo Electron's ongoing growth.