



Asset Value Investors

AN INDEPENDENT TOKYO RADIATOR

AVI's shareholder proposals to Tokyo Radiator Mfg. Co. Ltd.

May 2022

Introduction

Asset Value Investors (“AVI”) is the second-largest shareholder of Tokyo Radiator Mfg. Co. Ltd. (“Tokyo Radiator” or the “Company”), holding 5.2% of the shares.

AVI has submitted shareholder proposals for the Company’s 118th Annual General Meeting of Shareholders to be held in June 2022

For almost five years, as a long-term shareholder, AVI has been engaged with Tokyo Radiator; Marelli Corporation (“Marelli”), which holds approximately 40.1% of Tokyo Radiator’s shares; and Marelli’s parent company KKR, to resolve governance issues caused by Tokyo Radiator’s listed subsidiary structure and enhance Tokyo Radiator’s corporate value. AVI submitted shareholder proposals in June 2021 as part of its engagement activities. However, since then, Tokyo Radiator has continued to ignore AVI’s proposals and has made little effort to improve its weak governance.

In particular, AVI called on Tokyo Radiator to abolish the cash deposit system with Marelli, where approximately ¥4.1bn of cash, equivalent to 46.6% of Tokyo Radiator’s market capitalisation of ¥8.8bn, was lent to Marelli. AVI supports the return of the deposits to Tokyo Radiator but has nonetheless submitted shareholder proposals to ensure that such a practice is not reinstated again and that the deposits are returned to shareholders on an equal basis.

AVI asks its fellow minority shareholders to express their disapproval of the board of directors’ disregard for minority interests, by voting in favour of the shareholder proposals.



Overview of AVI's shareholder proposals

AVI's shareholder proposals to improve the weak governance of Tokyo Radiator

	Shareholder proposals	Outline
1	Special dividends equivalent to the past deposits to Marelli	Special dividends equivalent to the past deposits as of December 2021 to Marelli (~¥4.1bn in total, ¥284 per share)
2	Transition to the company with an Audit and Supervisory committee	Transition to a company with an Audit and Supervisory committee, where the Audit and Supervisory committee members have voting rights on the board of directors, thereby strengthening the supervisory function of the board of directors
3	Introduction of a Nomination Committee and a Compensation Committee	Abolishment of the current governance committee, chaired by the Representative Director, and establishment of a Nomination Committee and a Compensation Committee, chaired by an outside director and consisting of a majority of outside directors
4	Introduction of a restricted stock-based compensation scheme for directors	Introduction of a restricted stock-based compensation scheme for directors (excluding outside directors) that provides incentives to increase corporate value and promotes value sharing with shareholders
5	Abolishment of advisory roles (<i>Komon</i> and <i>Soudanyaku</i>)	Abolishment of advisory roles (<i>Komon</i> and <i>Soudanyaku</i>), as the current management team's consideration for the ex-management team's advice/opinion has had the detrimental effect on making them hesitant to make bold decisions

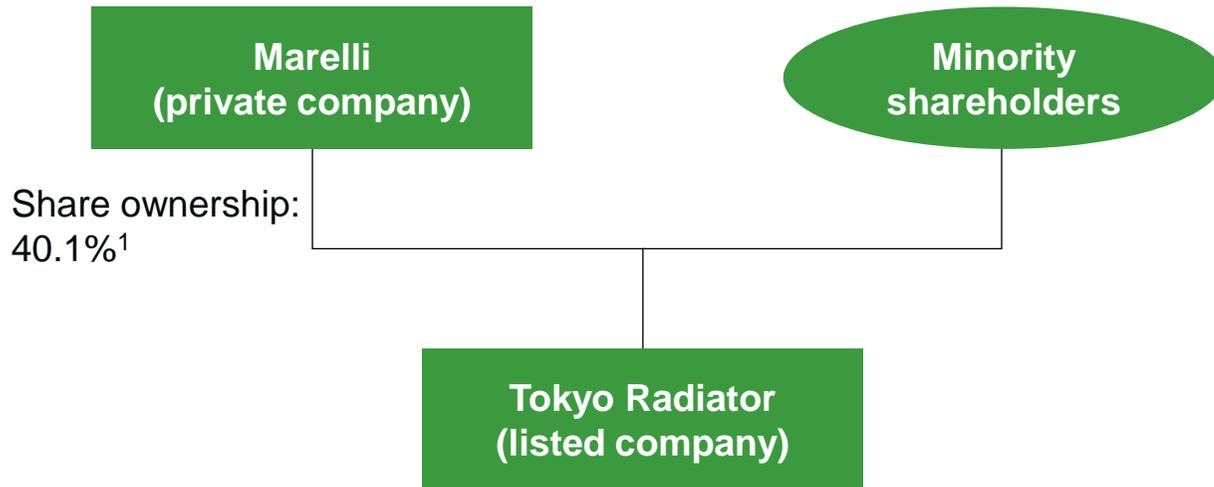


1 Special dividends equivalent to the past deposits to Marelli

Tokyo Radiator's listed subsidiary structure

Tokyo Radiator is a listed subsidiary in which Marelli owns 40.1%

Shareholder structure of Tokyo Radiator



Note 1: Tokyo Radiator, FY2022/03 Q2 quarterly report. The number of shares held as a percentage of the total number of shares issued (excluding treasury shares)

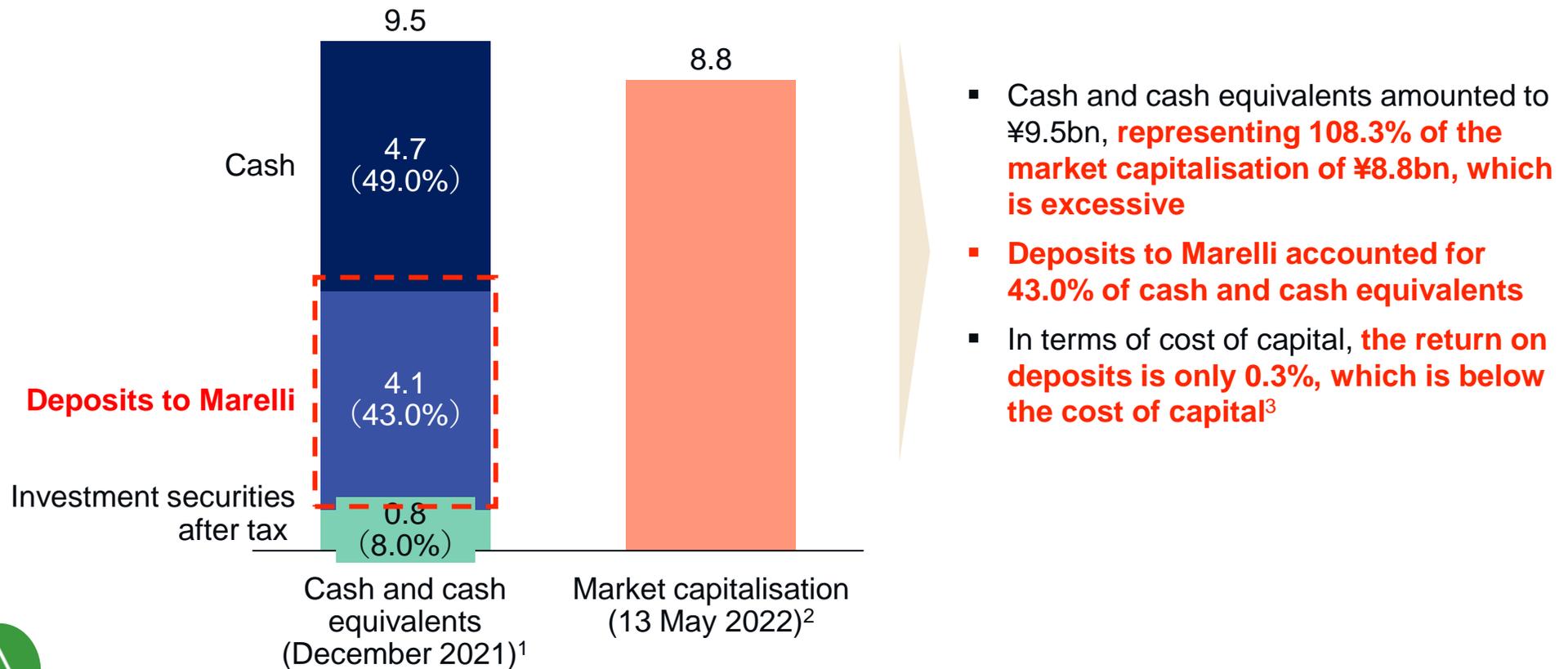


1 Special dividends equivalent to the past deposits to Marelli

Deposit system to Marelli

Tokyo Radiator had a huge amount of cash (¥4.1bn) on deposit to Marelli until just before Marelli filed for private debt reduction on 1 March 2022. The deposit system is a bad practice that provides Marelli with a cheap cash source and minority shareholders with a 0.3% return below its cost of capital

Cash and cash equivalents and market capitalisation of Tokyo Radiator (¥bn)



Note 1: Tokyo Radiator, FY2022/03 Q3 quarterly report. The tax rate applied to after-tax investment securities is 31%

Note 2: Capital IQ (as of 13 May 2022) Note 3: Tokyo Radiator, FY2021/03 annual report. Estimated based on interest income and deposits as stated in transactions with Marelli

1 Special dividends equivalent to the past deposits to Marelli

Conflict of interest structure due to deposits to parent company

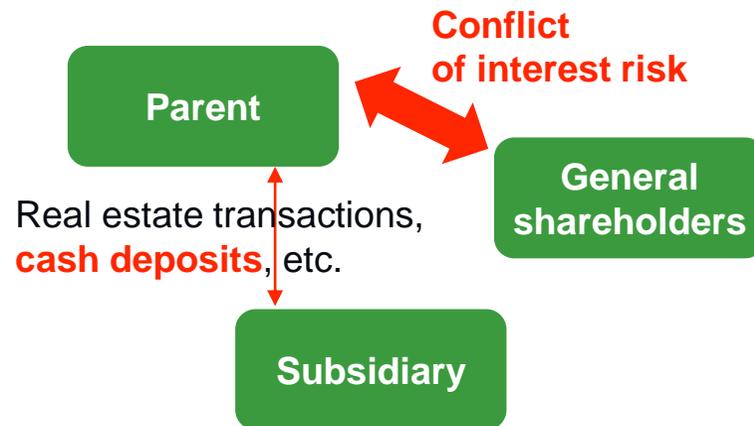
Deposits to the parent company pose a structural conflict of interest risk, as noted by the Ministry of Economy, Trade and Industry

Ministry of Economy, Trade and Industry "Practical Guidelines on Group Governance Systems"

【Conflict of Interest Structure of Listed Subsidiaries】

- In listed subsidiaries, there is a structural conflict of interest risk between the parent company (the controlling shareholder) and public shareholders of the listed subsidiary
- In situations where the following conflict of interest risks may materialize, the interests of general shareholders may be harmed. Therefore, it is necessary to give due consideration to the interests of general shareholders through the establishment of effective governance systems in listed subsidiaries

【Specific situation where conflict of interests may arise in listed subsidiaries】



Conflict of interests

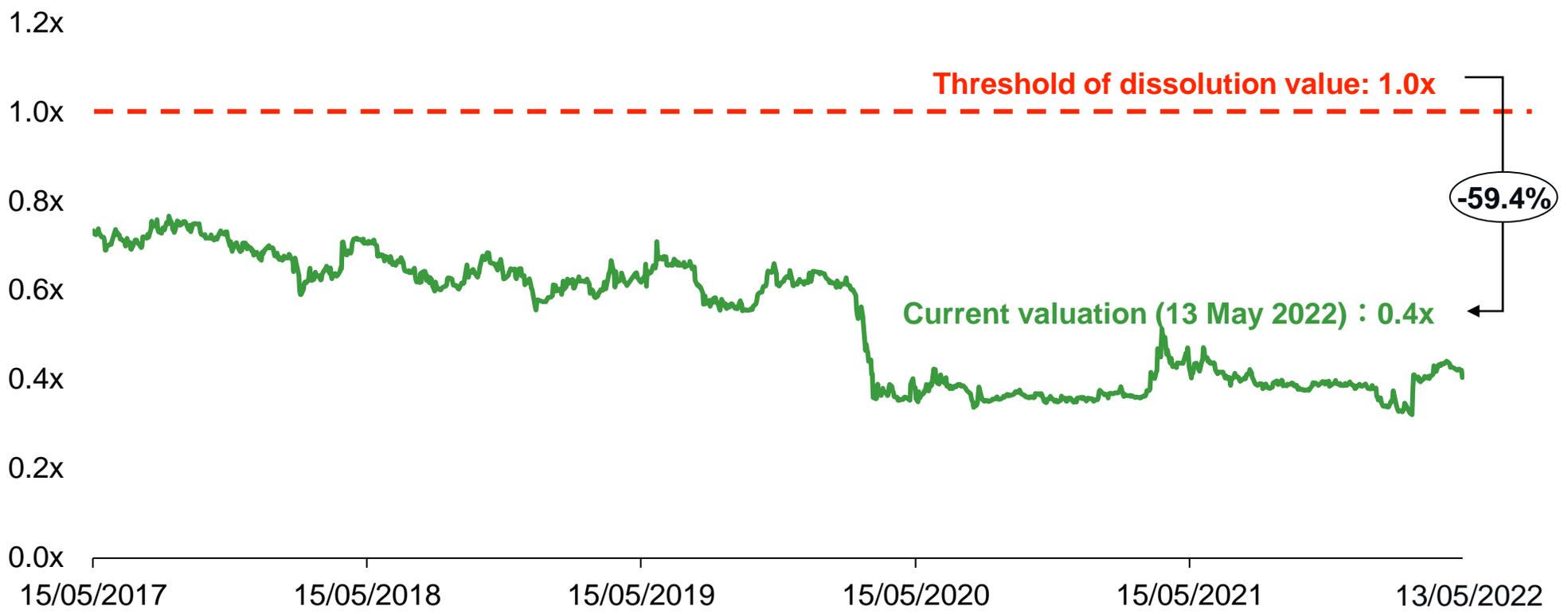
- Parent company wants to utilise subsidiary's cash at the lowest possible interest rate
- Subsidiary wants to use the cash for its own investments unless interest to meet its cost of capital is paid

1 Special dividends equivalent to the past deposits to Marelli

Valuation

Due to not utilising the deposits for its own benefit, Tokyo Radiator's price-to-book ratio (0.4x) is -59.4% below the dissolution value threshold of 1.0x

Price-to-book ratio of Tokyo Radiator (last 5 years)



Source: Capital IQ (as of 13 May 2022)



1 Special dividends equivalent to the past deposits to Marelli

Long-term underperforming parent company

Marelli is a long-term underperforming company that has posted final losses in the last four consecutive financial years. The Board of Directors breached its duty of care by continuing the deposit scheme to the long-term underperformer

Financial performance of Marelli

- **Marelli recorded losses for the past four fiscal years.** Marelli's final loss was ¥28.2bn in FY2020/12 and a multi-billion yen in FY2021/12¹
- On 1 March 2022, Marelli applied for the ADR process and requested **to reduce debts**²

Tokyo Radiator's deposits

- Tokyo Radiator recognised at the 2021 AGM that **it might not be able to recover its deposits in the event of Marelli's bankruptcy.** However, it continued to deposit cash to Marelli
- **Tokyo Radiator finally abolished the deposit system just before Marelli filed for the ADR process**

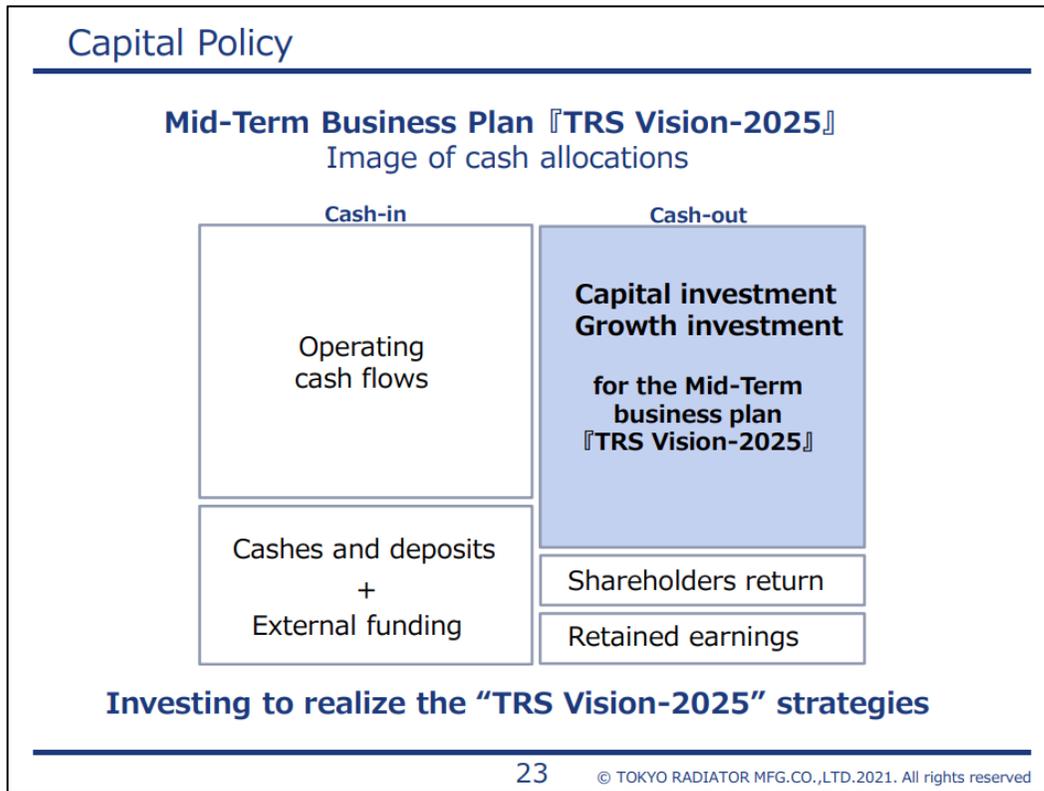
The Board of Directors breached its duty of care

Note 1: Nikkei (15 February 2022)
Note 2: Nikkei (1 March 2022)

Unclear capital policy

Tokyo Radiator does not disclose a quantitative investment plan. If there is no quantitative investment plan and the investment cannot exceed the cost of capital, then cash should be used to return to shareholders

Capital policy of Tokyo Radiator



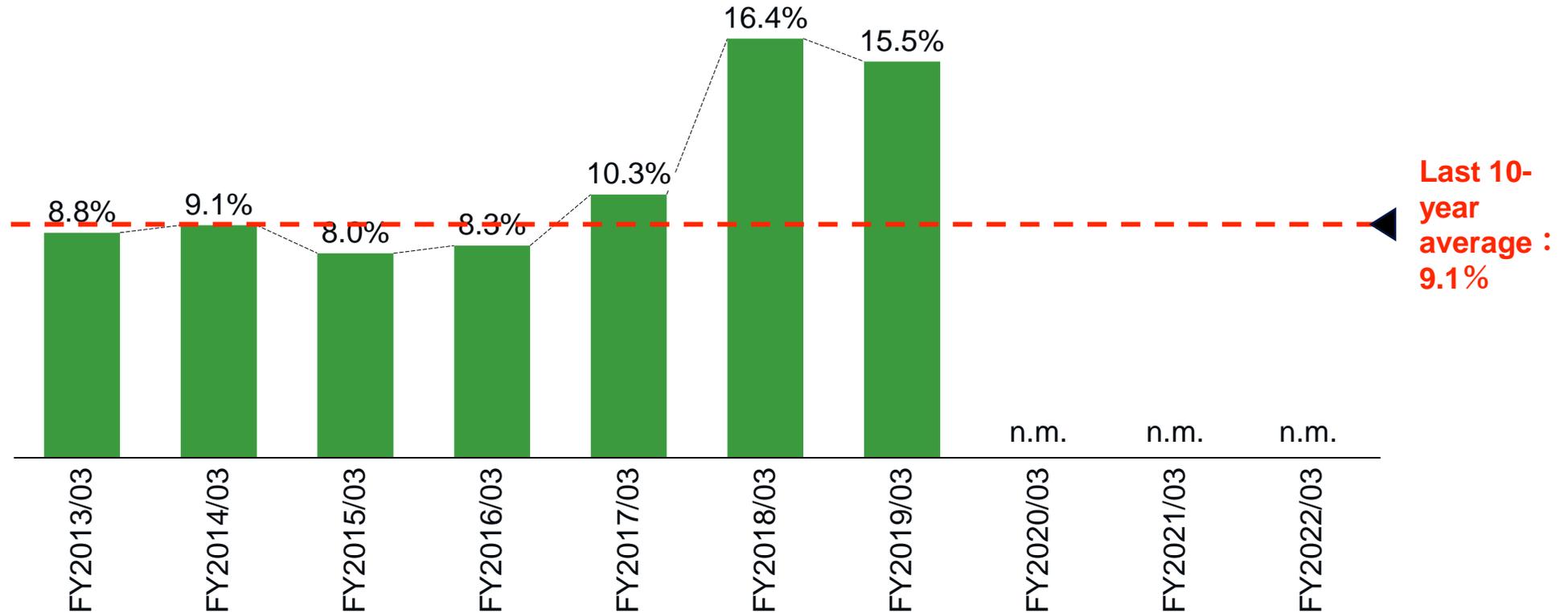
- While Tokyo Radiator has stated capital and growth investments for its medium-term management plan ‘TRS Vision-2025’, **there is no quantitative investment plan**
- If there is no quantitative investment plan and no investment to increase corporate value, **cash should be used for shareholder return**

1 Special dividends equivalent to the past deposits to Marelli

Insufficient shareholder return

Tokyo Radiator's dividend payout ratio over the past ten years is only 9.1%, and is reluctant to shareholder return

Dividend payout ratio of Tokyo Radiator (last 10 years)



Source: Tokyo Radiator, Kessan Tanshin (FY2013/03-FY2022/03)

Note: The dividend payout ratio for FY2020/03, FY2021/03 and FY2022/03 are not shown as they were outliers due to small net income of 238.1%, 101.4% and -14.4% respectively. Also, the average dividend payout ratio for the last 10 years does not include data for FY2020/03, FY2021/03 and FY2022/03

Shareholder Proposal ① : Special dividends equivalent to the past deposits to Marelli

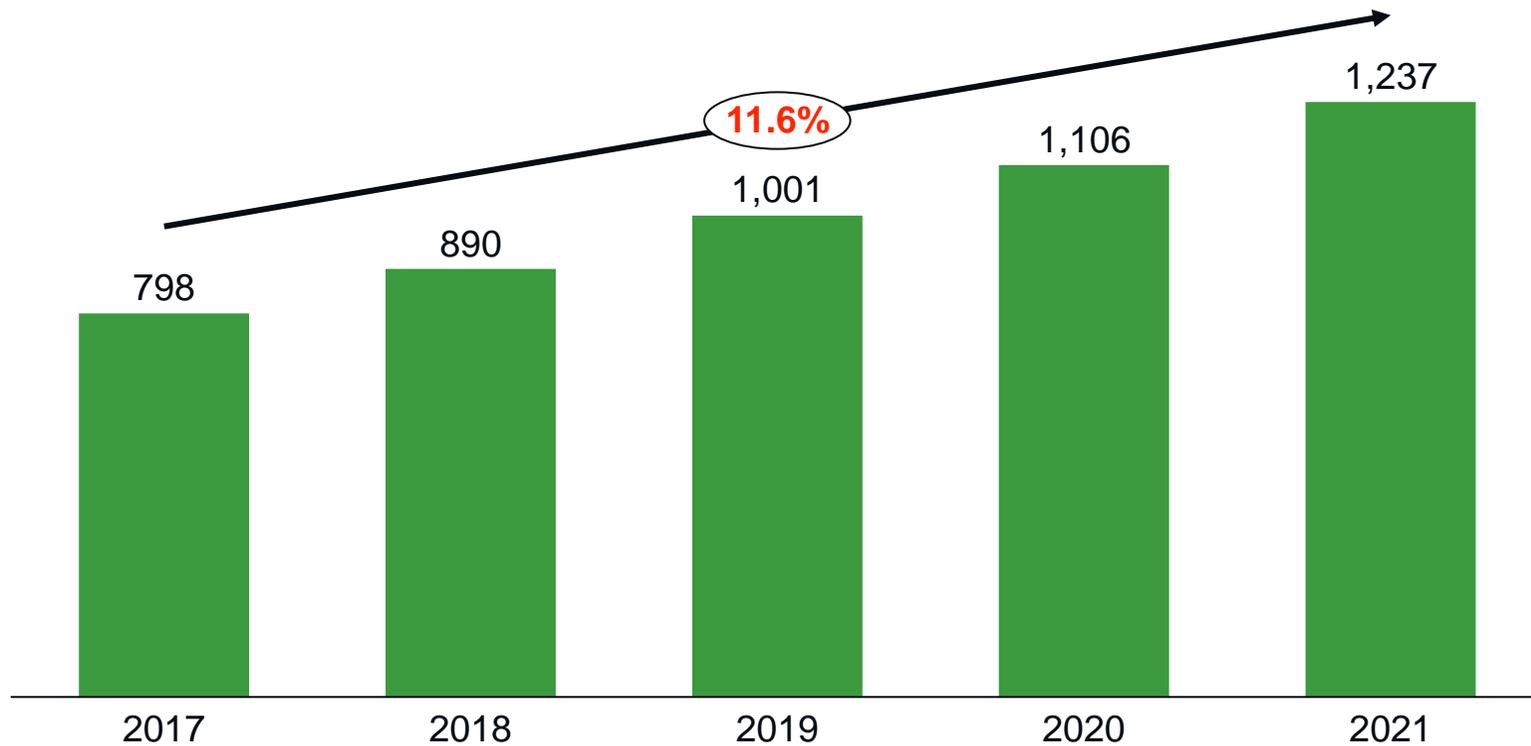
- Tokyo Radiator had deposited a large amount of cash with its parent company, Marelli. The deposit amounted to approximately JPY 4.1 billion at the end of December 2021, which corresponds to 46.6% of the market capitalisation of JPY 8.8 billion
- As pointed out in 'Practical Guidelines for Group Governance Systems' by the Ministry of Economy, Trade and Industry, the deposit system is a cheap source of funds for Marelli. The system benefits only Marelli at the expense of minority shareholders who suffer from a return on the cash investment far below Tokyo Radiator's cost of capital. Such conflict, in turn, leads to a low valuation (price-to-book ratio of 0.4x)
- While Marelli recorded losses for the past four fiscal years, Tokyo Radiator continued to deposit cash to Marelli until shortly before Marelli went into private debt reduction on 1 March 2022, despite the risk that the deposits would not be returned in the event of Marelli's bankruptcy. The continuation of the deposit system to such a poor-quality counterpart was a potential breach of duty of care by Tokyo Radiator's Board
- Looking at shareholder return, Tokyo Radiator's dividend payout ratio has averaged around 9.1% over the past ten years. Furthermore, the year-end dividend for FY3/2022 was zero. Tokyo Radiator has not disclosed a clear and quantifiable capital policy and it is therefore important for the corporate value and the common interests of its shareholders that the surplus funds generated by the abolition of these deposits are used to pay for the deficient shareholder return
- AVI is pleased that the deposit was since returned to Tokyo Radiator. However, to ensure that such a practice is not reinstated again and that the deposits are returned to shareholders on an equal basis, AVI proposes a special dividend (¥284 per share) equivalent to the deposits with Marelli at the end of December 2021 (approximately ¥4.1bn)

2 Transition to the company with an Audit and Supervisory Committee

Increase in companies with an Audit and Supervisory committee

Although Tokyo Radiator has the Board of Auditors, against a background of increased awareness of the need to strengthen corporate governance, the number of companies with an Audit and Supervisory committee has been increasing

The number of companies with an Audit and Supervisory committee



Source: Tokyo Stock Exchange, Inc. "Status of appointment of independent external directors and establishment of Nomination Committees and Compensation Committees in TSE-listed companies"



2 Transition to the company with an Audit and Supervisory Committee

The Board of Directors and the Board of Auditors

The Board of Directors includes Mr Ochiai, who is from Marelli, and the Board must pay attention to any resolutions affecting minority shareholders adversely in respect of Marelli's interests

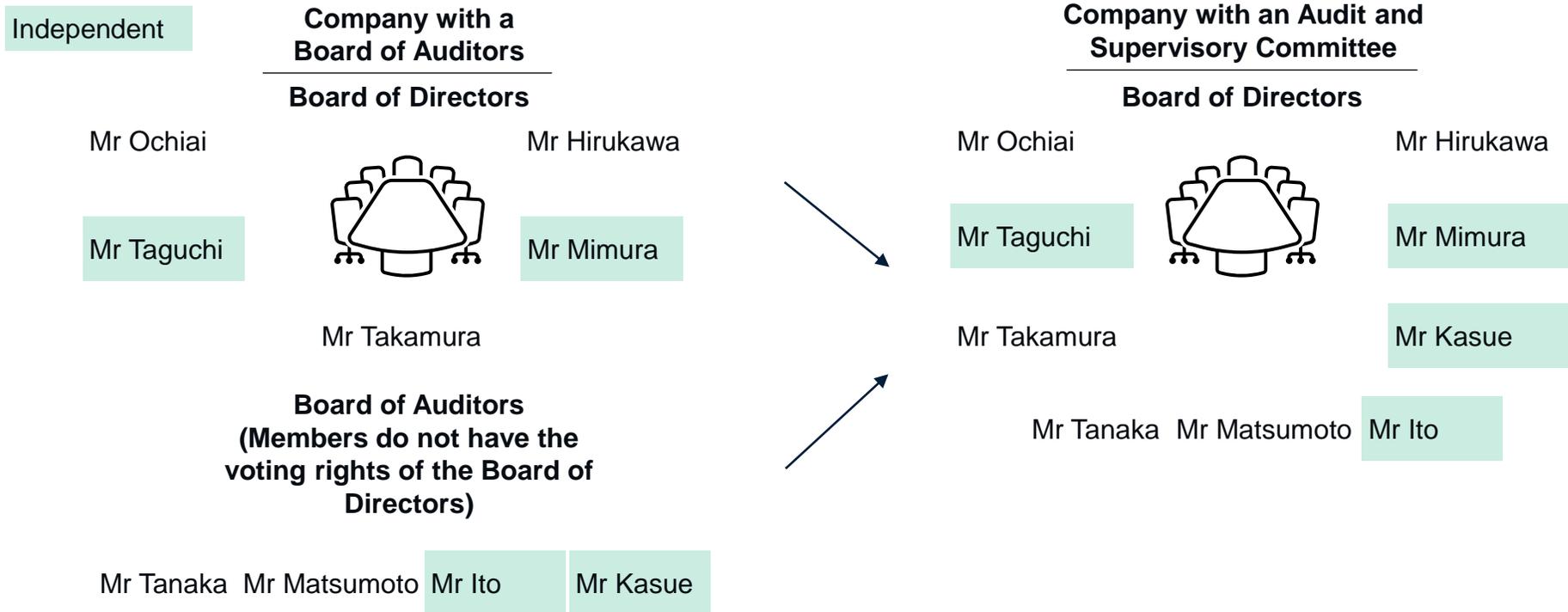
The Board of Directors and the Board of Auditors of Tokyo Radiator

	Title	Background	
The Board of Directors	Mr Hisao Ochiai	Representative Director	Marelli (Ex-Senior Vice President)
	Mr Kouji Hirukawa	Internal Director	Isuzu Motors Ltd.
	Mr Kenji Mimura	Internal Director	Tokyo Radiator
	Mr Youichi Taguchi	Independent Outside Director	Mitsubishi Metal Mining Company Ltd., etc.
	Mr Fujitoshi Takamura	Independent Outside Director	Komatsu Ltd.
The Board of Auditors	Mr Ryoichi Matsumoto	Internal Auditor	Tokyo Radiator
	Mr Akira Tanaka	Internal Auditor	Tokyo Radiator
	Mr Takaharu Ito	Independent Outside Auditor	Citibank, N.A., etc.
	Mr Yousuke Kasue	Independent Outside Auditor	Nissan Motor Co., Ltd.

2 Transition to the company with an Audit and Supervisory Committee

Company with an Audit and Supervisory Committee

A company with an Audit and Supervisory Committee can strengthen the supervisory function of the board of directors, as audit committee members can become members of the board and exercise voting rights



Tokyo Radiator's arguments on governance

Tokyo Radiator argues on the effectiveness of the current governance system of the company with the Board of Auditors. AVI has requested several interviews with directors to investigate the effectiveness of the governance system, but each request has been refused. This reluctance to engage in dialogue with shareholders in itself raises doubts about the effectiveness of its governance system

Tokyo Radiator's arguments on governance

The Company believes that the transition to a company with an Audit and Supervisory committee does not necessarily lead to stronger corporate governance.

The Company has established the DOA Regulations (Delegation of Authority) and delegates appropriate decision-making authority to each meeting body so that long-term strategies and other matters are fully discussed at the Board of Directors' meetings.

The two external directors have a wealth of experience and knowledge from other companies. They actively offer their opinions at the Board of Directors' meetings, including making proposals for the future. The full-time auditor attends management meetings and other major internal meetings to make comments as appropriate and monitor the executive side of the Company, and also conducts accurate audits in cooperation with the Company's internal audit office. The full-time auditors also monitor the executive side of the Company by attending major internal meetings such as the management committee and making comments as appropriate. Each auditor is independent and has strong auditing authority, as they can exercise authority independently, and the Board of Auditors is independent of the Board of Directors, which means that more rigorous auditing can be expected. **The Company believes that the auditing system of a company with a Board of Auditors is effective as a management monitoring function.**

Source: Tokyo Radiator "Notice of receipt of written correspondence on shareholder proposals and the Company's response" (May 2021)

Shareholder Proposal ② : Transition to the company with an Audit and Supervisory Committee

- Although Tokyo Radiator has the Board of Auditors, the number of companies with an Audit and Supervisory committee has been increasing (798 companies in 2017 and 1,237 companies in 2021)
- A company with an Audit and Supervisory Committee can strengthen the supervisory function of the board of directors, as audit committee members can become members of the board and exercise voting rights
- The Board of Directors includes Mr Ochiai, who is from Marelli, and the Board must pay attention to any resolutions affecting minority shareholders adversely in respect of Marelli's interests
- Tokyo Radiator argues on the effectiveness of the current governance system of the company with the Board of Auditors. AVI has requested several interviews with directors to investigate the effectiveness of the governance system, but each request has been refused. This reluctance to engage in dialogue with shareholders in itself raises doubts about the effectiveness of the governance system
- AVI proposes that Tokyo Radiator should move from a company with a Board of Auditors to a company with an Audit and Supervisory Committee to increase the effectiveness of the directors' supervisory function and improve the governance system

3 Establishment of a Nomination Committee and a Compensation Committee

Determination of director candidates and director compensation

Tokyo Radiator has entrusted Mr Ochiai, the Representative Director and the Chairperson of the Board with the responsibility of appointing candidates for the Board of Directors to be proposed to the AGM and determining the compensation of each director

Procedure for appointing candidates for the Board of Directors

Each year, **the Representative Director selects the candidates** and submits a proposal to the General Meeting of Shareholders for approval.

Source: Tokyo Radiator, corporate governance report (20 January 2022)

Procedure for determining the compensation of directors and auditors

The amount of compensation is determined within the total amount of compensation set by the resolution of the General Meeting of Shareholders. **The amount of remuneration for each director is determined by the Representative Director authorised by the Board of Directors in accordance with the Company's established policy**, while the amount of compensation for each auditor is determined through discussions by the Board of Auditors. The Governance Committee is consulted on basic matters concerning the remuneration of directors and auditors.

Source: Tokyo Radiator, corporate governance report (20 January 2022)

3 Establishment of a Nomination Committee and a Compensation Committee

Governance Committee

The Governance Committee advises on director candidates and directors' compensation. However, the Governance Committee is chaired by the Representative Director, who has been entrusted with the responsibility for director candidates and director compensation, which means that the Governance Committee is not independent

Governance committee of Tokyo Radiator

	現職	経歴
Mr Hisao Ochiai	Representative Director	Marelli (Ex-Senior Vice President)
Mr Youichi Taguchi	Independent Outside Director	Mitsubishi Metal Mining Company Ltd., etc.
Mr Fujitoshi Takamura	Independent Outside Director	Komatsu Ltd.
Mr Takaharu Ito	Independent Outside Auditor	Citibank, N.A., etc.
Mr Yousuke Kasue	Independent Outside Auditor	Nissan Motor Co., Ltd.

3 Establishment of a Nomination Committee and a Compensation Committee

Request for a Nomination Committee and a Compensation Committee

Establishment of a Nomination Committee and a Compensation Committee is requested by the Corporate Governance Code

Corporate Governance Code

Supplementary principle 4.10.1

If the organizational structure of a company is either Company with Kansayaku Board or Company with Supervisory Committee and independent directors do not compose a majority of the board, in order to strengthen the independence, objectivity and accountability of board functions on the matters of nomination (including succession plan) and remuneration of the senior management and directors, **the company should seek appropriate involvement and advice from the committees, including from the perspective of gender and other diversity and skills, in the examination of such important matters as nominations and remuneration by establishing an independent nomination committee and remuneration committee under the board, to which such committees make significant contributions.**

Shareholder Proposal ③ : Establishment of a Nomination Committee and a Compensation Committee

- Tokyo Radiator has entrusted Mr Ochiai, the Representative Director and the Chairperson of the Board with the responsibility of appointing candidates for the Board of Directors to be proposed to the AGM and determining the compensation of each director
- The Governance Committee advises on director candidates and director compensation. However, the Governance Committee is chaired by the Representative Director, who has been entrusted with the responsibility for director candidates and director compensation, which means that the Governance Committee is not independent
- Establishment of a Nomination Committee and a Compensation Committee is requested by the Corporate Governance Code
- In order to clarify the process for determining the selection and dismissal of directors and the remuneration of directors, AVI proposes that Tokyo Radiator should establish a Nomination Committee and a Compensation Committee, the majority of which will consist of outside directors, and that each committee will be chaired by an outside director

Management compensation incentives

The Corporate Governance Code calls for management compensation to incentivise mid- to long-term business results

Corporate Governance Code

Principle 4.2 Roles and Responsibilities of the Board (2)

The board should view the establishment of an environment that supports appropriate risk-taking by the senior management as a major aspect of its roles and responsibilities. It should welcome proposals from the management based on healthy entrepreneurship, fully examine such proposals from an independent and objective standpoint with the aim of securing accountability, and support timely and decisive decision-making by the senior management when approved plans are implemented.

Also, **the remuneration of the management should include incentives such that it reflects mid- to long-term business results and potential risks, as well as promotes healthy entrepreneurship.**

Compensation system

The compensation system for directors of Tokyo Radiator is entirely based on monetary compensation, and it is difficult to say that it reflects and "incentivises" the "medium- to long-term company performance" and "potential risks" as requested by the Corporate Governance Code

Compensation system of Tokyo Radiator¹

Type of compensation		Evaluation
Monetary compensation	Fixed compensation	<ul style="list-style-type: none"> Overall judgment based on position, responsibilities, skills and experience
	Performance-linked compensation	<ul style="list-style-type: none"> Consolidated sales, profits and other results of the previous year Individual and divisional results

4 Introduction of a restricted stock-based compensation scheme for directors

Tokyo Radiator's arguments on its compensation system

In May 2021, Tokyo Radiator announced that it would discuss its own compensation, but since this announcement, there have been no changes to the compensation system and no public announcement has been made as to what discussions have taken place

Tokyo Radiator's arguments on its compensation system

We discuss what systems are appropriate for increasing corporate value as our own incentive system, including a restricted stock-based compensation system.

Source: Tokyo Radiator "Notice of receipt of written correspondence on shareholder proposals and the Company's response" (May 2021)

Shareholder Proposal ④ : Introduction of a restricted stock-based compensation scheme for directors

- The Corporate Governance Code requests that the management remuneration should reflect and 'incentivise' 'medium- and long-term company performance' and 'potential risks'
- However, Tokyo Radiator's director compensation are paid only in monetary compensation and the criteria for the decision-making are " each director's position, responsibilities, skills and experience" as well as "consolidated sales, profit and other performance in the previous year, and the percentage of achievement of individual and departmental performance targets". They are far from the criteria required by the Corporate Governance Code
- Tokyo Radiator announced that it would discuss its own compensation system in May 2021, however no changes have been made nor has a public announcement been made as to what discussions have taken place
- AVI proposes a restricted stocks compensation scheme with a maximum annual amount of JPY 13 million for directors (excluding outside directors). The introduction of restricted stock compensation will increase the linkage of compensation to mid- to long-term performance and provide a sound incentive for directors to sustainably increase corporate value and promote further value sharing with shareholders. Furthermore, the adoption of a restricted stock compensation scheme will also ensure transparency in the compensation decision-making process

5 Abolishment of advisory roles (Komon and Soudanyaku)

Advisory roles (Komon and Soudanyaku)

Mr Hayashi, who retired as Chairman in June 2021, was appointed as an advisory role (Soudanyaku). Several other members of the management team were also appointed as advisers (Komon) on the same day. Although it is disclosed that Mr Hayashi is not involved in the management of the company, Tokyo Radiator confirmed to AVI that at the present time the agenda and reports of the Board of Directors are still shared with Mr Hayashi and he advises on these matters

Advisory role Soudanyaku of Tokyo Radiator

【代表取締役社長等を退任した者の状況】

(Status of persons who have retired from the Representative Director, etc.)

元代表取締役社長等である相談役・顧問等の氏名等

(Names, etc. of Soudanyaku and Komon, etc. who are former CEOs, etc.)

氏名 (Name)	役職・地位 (Position)	業務内容 (Business description)	勤務形態・条件 (常勤・非常勤、報酬有無等) (Type and conditions of work)	社長等退任日 (Date of resignation of the President, etc.)	任期 (Term)
林 隆司 (Takashi Hayashi)	相談役 (Soudanyaku)	これまでの経験を活かし、後進の指導・育成にあっております。(経営非関与) (Use of previous experience to guide and train younger staff (not involved in management))	非常勤・報酬有(定額) (Part-time, remunerated (fixed compensation))	2021/6/25 (25 June 2021)	1年 (1 year)

Harmful effects of advisory roles on management

The Ministry of Economy, Trade and Industry's Practical Guidelines on Corporate Governance System also points out the harmful effects of undue influence on the current management team when a former president or CEO remains as an advisory role

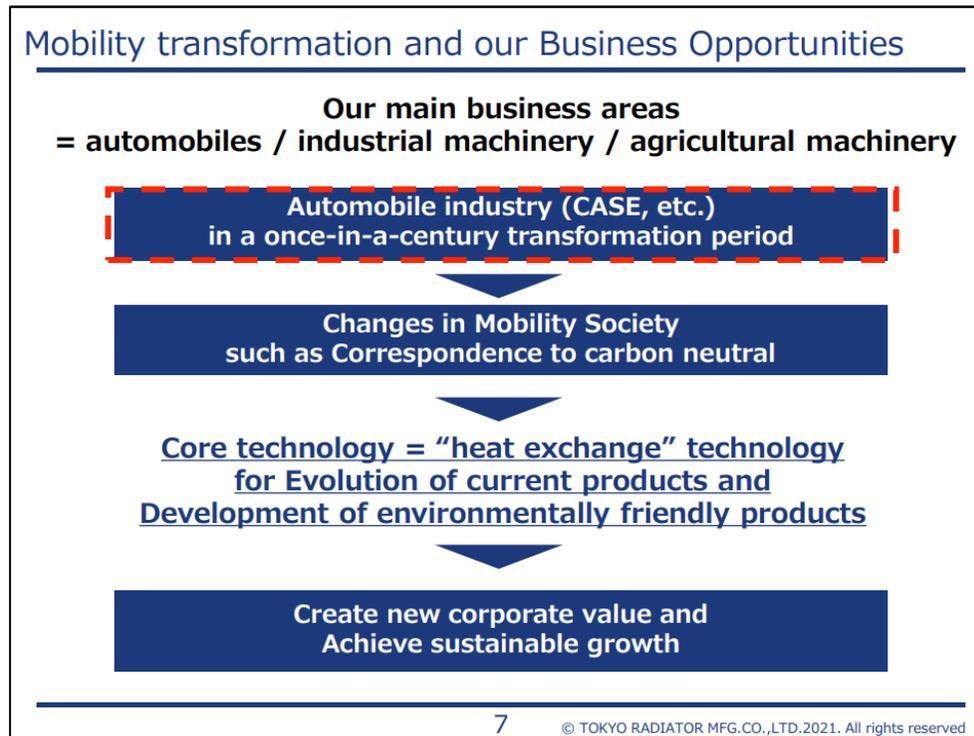
Ministry of Economy, Trade and Industry, “Practical Guidelines for Corporate Governance System

5.1.1. Issues with the Advisor/Consultant System

It is pointed out that **if a former president/CEO remains at his/her company as an advisor/consultant, the advisor/consultant who has no responsibility for company management may exercise unreasonable influence over incumbent management members, and that there may arise a harmful effect that who is actually taking the management leadership is not clear.** It is also pointed out that **even if an advisor/consultant does not actively exercise unreasonable influence, the advisor/consultant may still be a factor causing the current management to hesitate to make bold decisions, such as the reconstruction of business portfolios, when the current management are apprehensive about the intention of the advisor/consultant who was a previous president/CEO**

Current management needs to make bold decisions

As mentioned in the medium-term management plan, it is necessary for the current management team to make bold decisions without regard to the opinions of advisors to respond to the wave of change in the “automobile industry, which is undergoing a once-in-a-century transformation”



Shareholder Proposal ⑤ : Abolishment of advisory roles (Komon and Soudanyaku)

- Mr Takashi Hayashi, who retired as the Chairman of the Board of Directors in June 2021, was appointed as a Soudanyaku. Several other members of the management team were also appointed as Komon on the same day. Tokyo Radiator discloses that Mr Takashi Hayashi is not involved in company management. However, at the present time, the agenda items and reports of the Board of Directors are shared with Mr Hayashi and he advises on them
- The Ministry of Economy, Trade and Industry's "Practical Guidelines on Corporate Governance Systems" points out that the adverse effect of undue influence on the current management team has been noted when people with experience as president/CEO remain as Komon or Soudanyaku
- As mentioned in the medium-term management plan, it is necessary for the current management team to make bold management decisions without regard to the opinions of advisors and consultants in order to respond to the wave of change in the 'automobile industry, which is undergoing a once-in-a-century transformation'
- Therefore, AVI proposes that Tokyo Radiator should abolish the positions of Komon and Soudanyaku

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