Practical Handbook for ESG Disclosure

JAPAN EXCHANGE GROUP, INC.
TOKYO STOCK EXCHANGE, INC.

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Introduction

Background to the Handbook

In recent years, a large range of investors have come to acknowledge that when evaluating a company's corporate value from a mid- to long-term perspective, it is important to take into account the "sustainability" of the company's operations, including ESG (Environment, Social, Governance) factors. Listed companies have also begun to act on starting ESG-related activities and improving ESG-related information disclosure (hereinafter referred to as "ESG disclosure"), as part of their accountability towards investors and other stakeholders.

In line with this trend, a number of standards, frameworks and guidance documents (hereinafter collectively referred to as "frameworks") have been provided by governments, international organizations, stock exchanges, NGOs and others to help companies with ESG disclosure. Although most of these have been from outside Japan, the Japanese Ministry of Economy, Trade and Industry has also published a Guidance for Integrated Corporate Disclosure and Company-Investor Dialogues for Collaborative Value Creation - ESG integration, non-financial Information disclosure and Intangible Assets into Investment ("Guidance for Collaborative Value Creation") and a Guidance for Climate-related Financial Disclosures ("TCFD Guidance").

However, while the range of frameworks that listed companies can refer to when looking into ESG disclosure has grown, listed companies have reported difficulties in telling the frameworks apart and confusion over how to use each one. Given that most of the frameworks are from outside Japan, many companies have also felt that there is not enough information about them in Japanese.

With this background, Japan Exchange Group, Inc. (JPX) has created this Handbook to support listed companies with their voluntary efforts to improve ESG disclosure, thereby encouraging dialogue between listed companies and investors.

Objective of the Handbook

JPX has been working to improve the value of its listed companies, for example through better corporate governance, for a number of years. Japan's Corporate Governance Code, created by Tokyo Stock Exchange and implemented in 2015, requires listed companies to address social, environmental and other sustainability issues positively and proactively, while the 2018 revision clarified that "non-financial information" should include ESG information, and called for companies to disclose this information in a valuable and useful way. The Code also requires listed companies to disclose information on governance (the "G" of ESG) in a

Corporate Governance Report.

In December 2017, JPX joined the Sustainable Stock Exchanges (SSE) Initiative, and in June 2019, it made and published a Japanese translation of the SSE Initiative's Model Guidance on Reporting ESG Information to Investors [1]. The Guidance brings together important issues regarding ESG disclosure as a result of discussions with its founding organizations and Partner Exchanges.

Having provided listed companies with the SSE Model Guidance, however, JPX felt that putting it into practice would require some more practical information. With this in mind, the Practical Handbook for ESG Disclosure aims to provide Japanese listed companies with helpful information to refer to when taking their first steps towards beginning ESG disclosure[2].

Important features of the Handbook

Below are some important features of this Handbook.

1. The Handbook aims to help listed companies which choose to link ESG issues to corporate value and disclose about those issues in a way that the links can be clearly understood. For that reason, rather than listing specific data points to disclose, it focuses on issues that listed companies come across when looking at ESG disclosure internally. These issues, along with related processes and other points to consider, are split into four Steps that companies can follow.
2. To encourage disclosure of information useful to investors for making investment decisions, the Handbook incorporates investors' points of view ("investors" in this Handbook means mainly asset owners (pension funds, etc.) and asset managers (financial advisors)).
3. Each Step in the Handbook has been chosen with reference to points common to existing frameworks. The relevant parts of each framework are then specified, making it easier for readers to refer back. The main frameworks that are referred to in the Handbook are as below (outlines of each can be found in the appendix):

- Sustainable Stock Exchanges (SSE) Initiative: Model Guidance on Reporting ESG Information to Investors ("SSE Model Guidance")
- Ministry of Economy, Trade and Industry (METI): Guidance for Integrated Corporate Disclosure and Company-Investor Dialogues for Collaborative Value Creation - ESG integration, non-financial information disclosure and intangible assets into investment ("Guidance for Collaborative Value Creation")
- Recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) ("TCFD Recommendations")
- Sustainability Accounting Standards Board (SASB) Standards

[1]Sustainable Stock Exchange Initiative (2015) "Model Guidance on Reporting ESG Information to Investors" <https://sseinitiative.org/wp-content/uploads/2017/06/SSE-Model-Guidance-on-Reporting-ESG.pdf>
[2]Similar ESG guidelines for listed companies have been published by other exchanges around the world, including London Stock Exchange, Deutsche Börse, Hong Kong Exchanges and Clearing, Singapore Exchange and NASDAQ.

- International Integrated Reporting Council (IIRC): International Integrated Reporting Framework ("IIRC Framework")
- Global Reporting Initiative (GRI) Standards
- World Federation of Exchanges (WFE): ESG Guidance and Metrics

4. To enable deeper understanding, each Step is illustrated with actual cases of disclosure, so that readers can form a realistic image of the processes involved.
5. The Handbook is designed so that rather than reading front to back, each company can choose which parts to refer to depending on their current circumstances.

Intended audience

The Handbook is mainly aimed at listed companies which are thinking of beginning ESG disclosure, but those who have already begun disclosure should also find some useful information.

The Handbook's intention is to provide information which can help companies to aim for improved corporate value through understanding ESG and ESG investment, working on ESG issues in a way that fits the company, and enacting dialogue with investors and other stakeholders. However, relevant ESG issues and their importance will differ from company to company, so we do not expect the processes and examples shown in this Handbook to fit perfectly to every company. We hope that by using the Handbook, listed companies can deepen their understanding of each Step and work on ESG disclosure with contents and methods that fit to their individual circumstances.

The four Steps that make up the Handbook

In order to effectively disclose the ESG-related information which investors need to evaluate mid- to long-term corporate value, it is important that rather than simply focusing on what specific points to disclose and how, companies can come to these decisions through a process of linking corporate value to ESG issues. The Handbook brings together the issues involved in this and splits them into the below four Steps. These Steps were chosen with reference to actual cases of disclosure, the Guidance for Collaborative Value Creation, the TCFD Recommendations, the IIRC Framework and others.

None of the Steps or processes are prescriptive or absolute, and listed companies can begin ESG disclosure without completing all of them perfectly. If companies begin ESG disclosure with whatever information their current circumstances allow, this will lead to dialogue with investors, which will then enable further actions. We hope that the Handbook can be used as a guide through all of these stages.

Step 1
ESG Issues and ESG Investment

1-1 Understanding ESG issues and ESG investment
-ESG and corporate value
-E, S, and G
-The rise of ESG investment
-ESG investment and fiduciary duty
-Investor diversity
-What investors are asking for
-ESG in the Corporate Governance Code
-ESG issues and your business

Step 2
Connecting ESG Issues to Strategy

2-1 ESG and its impact on strategy

2-2 Identifying what is "material"
-"Materiality" and ESG
-Why materiality is important
-Making a material issues longlist
-Evaluating the importance of ESG issues
-Material issues and strategy

The Handbook is made up of the below four Steps.

Step 1: ESG Issues and ESG Investment

Understand ESG issues and the current situation around ESG investment.

Step 2: Connecting ESG Issues to Strategy

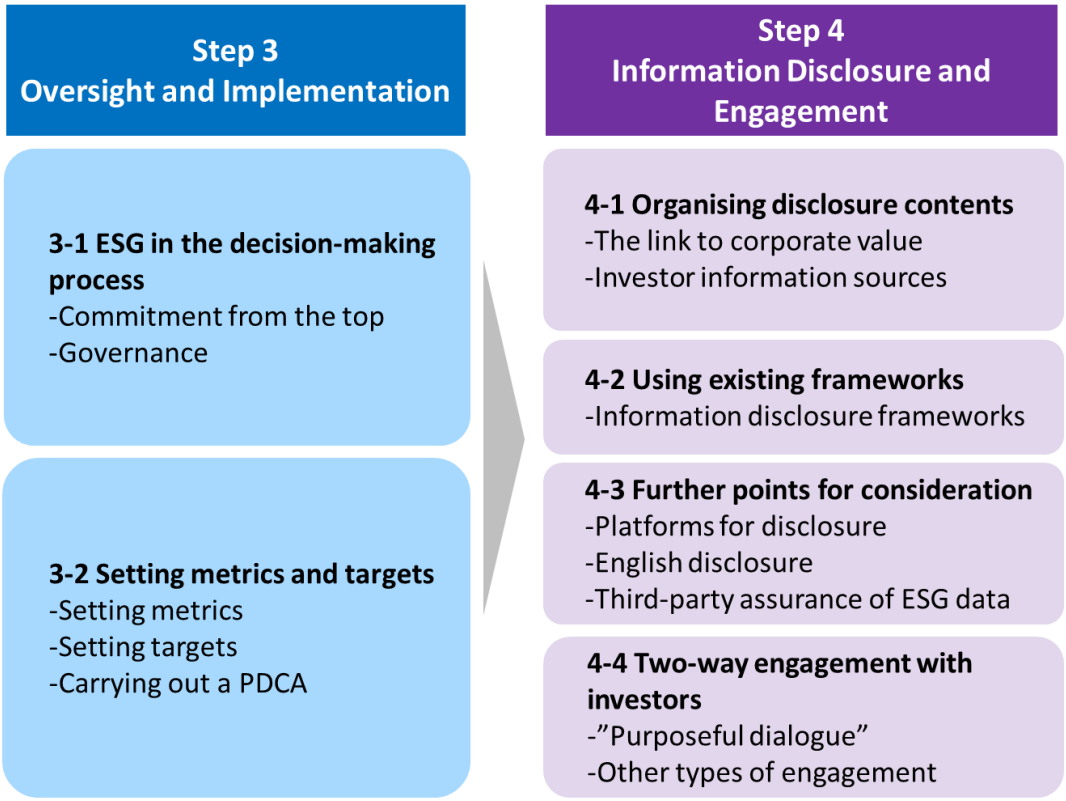
Decide on what ESG issues are "material" to your company's strategy.

Step 3: Oversight and Implementation

Put in place an internal structure for oversight and implementation of ESG issues and set metrics/targets, to enable steady progress on ESG activities.

Step 4: Information Disclosure and Engagement

Having linked ESG issues to corporate value, disclose ESG information so it can be used for investment decisions. Aim for mid- to long-term corporate value creation by actively seeking dialogue with investors and other stakeholders.



Step 1: ESG Issues and ESG Investment

For companies to aim for corporate value improvement through disclosing investment decision-useful ESG information and enacting dialogue with investors, it is important to first understand what ESG issues are and what the current situation is around ESG investment. This Step introduces trends around ESG investment.

Sections

1-1 Understanding ESG issues and ESG investment

- ESG and corporate value
- E, S, and G
- The rise of ESG investment
- ESG investment and fiduciary duty
- Investor diversity
- What investors are asking for
- ESG in the Corporate Governance Code
- ESG issues and your business

1-1 Understanding ESG issues and ESG investment

ESG and corporate value

When investors look to evaluate the corporate value of their investee companies, as well as using financial information such as balance sheets and profit and loss statements, they also refer to non-financial information. In recent years, awareness of ESG issues as a part of that non-financial information has grown, from the perspective of their impact on company sustainability and mid- to long-term corporate value. In this way, ESG issues have become much more important for investors' investment decisions and in company disclosure.

E, S, and G

ESG stands for Environmental, Social, and Governance, and is generally used to mean a wide range of issues connecting to those three themes. Although there is no universally agreed definition of ESG, a good example is the below list from the Principles for Responsible Investment (PRI)[3]:

- Environmental (E): climate change, resource depletion, waste, pollution, deforestation, etc.
- Social (S): human rights, modern slavery, child labour, working conditions, employee relations, etc.
- Governance (G): bribery and corruption, executive pay, board diversity and structure, political lobbying and donations. tax strategy, etc.

The rise of ESG investment

"ESG investment" is when an investor makes an investment decision taking into account company information relating to ESG issues as well as the traditional financial information. The term became known among investors from 2006, when then-UN Director General Kofi Annan led the formation of the PRI, which calls for investors to take into account ESG information in their investment decisions.

The number of institutional investors who have signed the PRI has been growing ever since, surpassing 2,860 worldwide as of January 2020[4]. At the same time, the amount of assets under management being allocated for ESG investment is also growing, from 22.8 trillion USD in 2016 to 30.6 trillion in 2018, according to a report from the Global Sustainable Investment Alliance (GSIA)[5].

ESG investment is also growing in Japan. The awareness and activity of domestic institutional investors has been shifting ever since the Government Pension Investment Fund (GPIF) signed the PRI in 2015, and the number of Japanese PRI signatories exceeded 80 in January 2020. According to the same GSIA report, the

[3] PRI website “What is responsible investment?” <https://www.unpri.org/pri/an-introduction-to-responsible-investment/what-is-responsible-investment>
[4] PRI website "PRI Signatories" <https://www.unpri.org/signatories>
[5] Global Sustainable Investment Alliance (2019) "2018 GLOBAL SUSTAINABLE INVESTMENT REVIEW" <http://www.gsi-alliance.org/wp-content/uploads/2019/03/GSIR_Review2018.3.28.pdf>

amount of Japanese assets allocated to ESG investment more than tripled between 2016 and 2018, from 0.5 trillion USD to 2.1 trillion (18.3% of all assets under management).

More recently, a number of other publications and events have provided a further tailwind for ESG, including the UN's Sustainable Development Goals (SDGs), the Paris climate conference (COP21), and the Financial Stability Board's (FSB) Task-force on Climate-related Financial Disclosures (TCFD).

ESG investment and fiduciary duty

One piece of context about the growth of ESG investment concerns how it was made possible within the framework of fiduciary duty, an obligation which most institutional investors have to their customers.

The trigger for this was again the PRI, launched in 2006. The PRI puts into writing the connection between ESG and fiduciary duty, with signatories agreeing that "As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios... Therefore, where consistent with our fiduciary responsibilities, we commit to the [6 principles]."

The issue has been debated in Europe and the US since then in the context of fiduciary duty regulations for pension fund operators, and although countries differ on some points, regulation has at least made it possible for ESG to be considered by investors, not to give social responsibility preference over investment returns, but as a part of ensuring those returns.

In the case of Japan, in 2014 the Stewardship Code was launched as "principles for a wide range of institutional investors to appropriately discharge their stewardship responsibilities, with the aim of promoting sustainable growth of investee companies, through constructive dialogue with them". The Code states that "Institutional investors should monitor investee companies so that they can appropriately fulfill their stewardship responsibilities with an orientation towards the sustainable growth of the companies", and that factors for monitoring "may include, for example, the investee companies' governance, strategy, performance, capital structure, business risks and opportunities (including risks and opportunities arising from social and environmental matters), and how the companies address them."

The Stewardship Code's 2020 revision goes further, specifying that a part of stewardship responsibility is purposeful dialogue with companies based on in-depth knowledge of not just companies and their business environment, but "consideration of sustainability (medium- to long-term sustainability including ESG factors) consistent with their investment management strategies."

In this way, a growing number of Japanese institutional investors now see it as an important part of fulfilling their fiduciary duty and accountability as investors to consider ESG factors when making investment decisions and report this process and its results to asset owners or beneficiaries.

Inset 1.1: The EU sustainable finance strategy

The EU is laying foundations to promote sustainable finance at a regulatory level.

On the topic of reporting of non-financial information, in October 2014 the EU announced the "non-financial reporting Directive (2014/95/EU)" which sets out rules on disclosure of non-financial and diversity information by large EU-based companies, and was applied from fiscal years beginning in 2017. To support this Directive, the EU also released "Guidelines on non-financial reporting" in June 2017. Through these, the EU is supporting more consistent and comparable disclosure of non-financial information[6]. Guidelines on reporting climate-related information were also added in June 2019.

In addition, to encourage private capital flows into sustainable projects such as those combating climate change, in March 2018 the European Commission (EC) launched an "Action plan on financing sustainable growth"[7]. A technical expert group was set up to debate the issues, and in June 2019 this group published reports on 1) an EU taxonomy (definitions of and a classification system for sustainable economic activity in the EU), 2) an EU Green Bond Standard, and 3) sustainable benchmarks (stock indices)[8]. The EU taxonomy, currently focusing on climate change mitigation and adaptation, is intended to form the basis of EU sustainable finance and will eventually be wired into regulations on capital requirements for banks and investment activities, as well as standards for financial products and other rules. These new rules are aimed not just at promoting sustainable finance, but also attaining the goals of the SDGs and the Paris Agreement (keeping a global temperature rise this century well below 2 degrees Celsius above pre-industrial levels)[9].

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[6] European Commission website "Commission guidelines on non-financial reporting" <https://ec.europa.eu/info/publications/non-financial-reporting-guidelines_en>

[7] European Commission website "Commission action plan on financing sustainable growth" https://ec.europa.eu/info/publications/180308-action-plan-sustainable-growth_en

[8] European Commission website "Technical expert group on sustainable finance (TEG)" <https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en>

[9] European Commission website "Sustainable finance: Commission publishes guidelines to improve how firms report climate-related information and welcomes three new important reports on climate finance by leading experts" <https://europa.eu/rapid/press-release_IP-19-3034_en.htm>

Investor diversity

Although "ESG investment" is used as a catch-all phrase, in fact it encompasses a range of investment strategies, objectives, timelines and other factors, all of which require different ESG information and use it in different ways. GSIA have created the below guide which splits ESG investment strategies into 7 types[10]. According to GSIA's statistics, the most practiced strategy in Japan is "Corporate engagement and shareholder action", followed by "ESG integration". In fact, in Japan's case, engagement and shareholder action (e.g. exercising voting rights) is being seen not just in active investment, where investee companies are chosen by evaluating each of them according to a specific investment strategy, but also in passive investment, where investors use a stock index such as TOPIX as a benchmark. A trend has been seen recently for indices which include ESG factors in their calculation methods. With ESG investment and its related investment strategies spreading, the range of uses for ESG information is increasing in turn.

As for why investors are turning to ESG investment, a survey by the Ministry of Economy, Trade and Industry[11] showed that 97.9% of investors surveyed (all those who were practicing ESG investment) aimed to "Reduce risks", while 87.5% wanted to "Increase returns", 83.3% said it was to "Contribute to society", and 20.8% replied "Other".

With this knowledge about the diversity of investors, it is important to look into ESG disclosure while thinking about who you are disclosing for and what kind of information they need.

Types of ESG investing

	Description
Negative screening	The exclusion from a fund or portfolio of certain sectors, companies or practices based on certain ESG criteria
Positive screening (best-in-class)	Investment in companies selected for positive ESG performance relative to industry peers
Norms-based screening	Screening of investments against international norms, such as those issued by the OECD, ILO, UN and UNICEF
ESG integration	The inclusion of environmental, social and governance factors into financial analysis
Sustainability themed investing	Investment in themes or assets related to sustainability (e.g. clean energy, green technology or sustainable agriculture)
Impact/community investing	Targeted investments aimed at solving social or environmental problems
Corporate engagement and shareholder action	Influencing corporate behaviour through engagement, shareholder proposals, and proxy voting using ESG guidelines

Source: GSIA (2019) "2018 Global Sustainable Investment Review" (edited)

[10] See footnote 5

[11] Ministry of Economy, Trade and Industry (2019) "Questionnaire Survey for Fund Management Organizations on ESG Investment" (Japanese only) <https://www.meti.go.jp/press/2019/12/20191224001/20191224001-1.pdf>

Inset 1.2: An example of a company valuation using ESG information[12]

Asset manager A has created a framework for integrating ESG information into valuations of corporate value (ESG integration) by selecting different ESG factors for each sector (e.g. CO2 footprint for energy companies, labour standards or product safety for retail companies), and has embedded that framework into its fundamental analysis. While A finds it hard to quantify the social and environmental risks of holding a stock, it tries to evaluate a company's position and outlook by performing a sensitivity analysis to obtain a range of possible fair values.

This is an example of an ESG analysis that A performed on sports equipment manufacturer X.

After years of dialogue with X, A found gradual improvements in the company's risk management and labour standards. A was able to then embed these positive changes into its valuation model through future cash flows and the discount rate, as below.

1. A positive impact on future cash flow

   As A believes that there is a positive correlation between revenue and social factors such as employee satisfaction, it expects a company with a highly motivated labour force to have a better sales performance. To take into account the positive implication on sales and cash flows, A increased the market estimates of sales growth by 1% per year.

2. A positive impact on the long-term discount rate through lower reputational risk

   A considers that a company with good risk management can limit its reputational risk compared to its peers. To reflect this positive impact in its company evaluation, A decreased the discount rate by 0.5%.

Asset manager A's evaluation of sports equipment maker X

(factors that affect corporate value)

	Short term	Long term
Affecting future cash flow	• Quarterly expectations • Leading indicators, KPIs • Foreign exchange movements	• Sustainability of operations ↑ • Sustainability of business model • Management quality • Internal growth • Valuation
Affecting the discount factor	• Technicals • Sentiment • Volatility	• ESG reputational risk ↓ • Equity risk premium • Credit market • Regulatory risk

[12] Based on a case study in PRI (2016) "A PRACTICAL GUIDE TO ESG INTEGRATION FOR EQUITY INVESTING" <https://www.unpri.org/listed-equity/a-practical-guide-to-esg-integration-for-equity-investing/10.article>

Inset 1.3: The rise of millennials

One thing cited as a boost to the growth of ESG investment is the rise of the millennial generation (those born between the early 1980s and the mid-1990s). Millennials pay more attention to environmental and social issues than previous generations, and they are already well known as consumers for choosing products and companies which contribute to solving social issues. By extension, there is also evidence showing a high level of interest in ESG investment among millennials[13], as awareness grows that they can make a difference to issues such as climate change and the elimination of poverty through investment choices. Some financial institutions are now looking to develop and provide financial products to cater for this trend.

Inset 1.4: TCFD and Japan's Green Investment Guidance

The E (environmental) of ESG, above all climate change, is gaining attention across the world as a vital issue that needs to be acted on. The financial sector is no different. In 2015, seeing a high probability that climate change will destabilise financial markets, the Financial Stability Board (FSB) set up the Task Force on Climate-related Financial Disclosures (TCFD) to begin debating the impact it could have on the sector and the necessary response. The TCFD Recommendations, published in June 2017, have been taken up by companies and organisations globally, with the number of organisations having announced their support at 983 as of January 2020[14]. Of individual countries, Japan has the most TCFD supporters, with 228 as of January 2020.

In Japan, a "TCFD Consortium" was set up in May 2019 as a platform to discuss how to improve the effectiveness of disclosure based on TCFD and how investors can reflect this information in their investment decisions. The Guidance for Utilizing Climate-related Information to Promote Green Investment (Green Investment Guidance)[15], which the Consortium released in October 2019, contains advice for investors on how to interpret and use disclosed information based on the TCFD Recommendations. It can be a useful reference for companies wanting to understand the investor point of view.

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[13] Morgan Stanley Institute for Sustainable Investing (2017), "Sustainable Signals New Data from the Individual Investor" <https://www.morganstanley.com/pub/content/dam/msdotcom/ideas/sustainable-signals/pdf/Sustainable_Signals_Whitepaper.pdf>

[14] TCFD website "Supporters" <https://www.fsb-tcfd.org/tcfd-supporters/>

[15] TCFD Consortium (2019) The Guidance for Utilizing Climate-related Information to Promote Green Investment ("Green Investment Guidance") <https://www.tcfd-consortium.jp/en/news_detail/19100802>

What investors are asking for

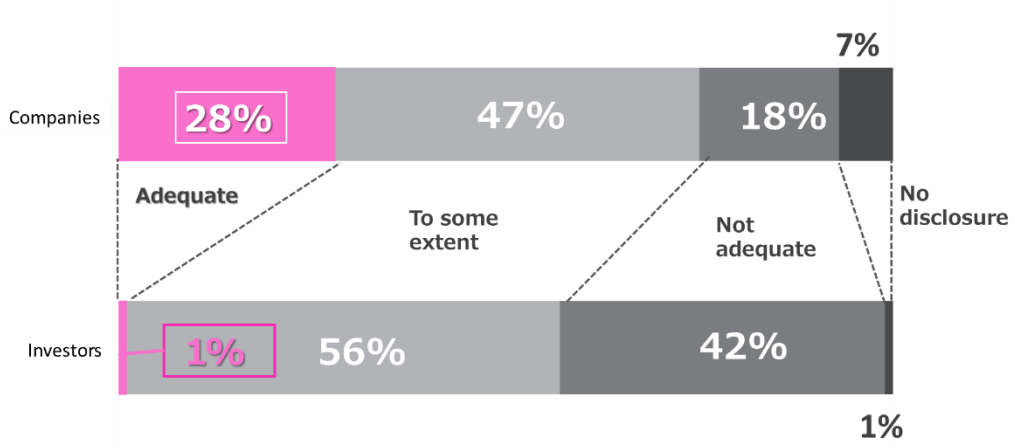
As ESG investment grows, requests to listed companies from investors for ESG disclosure are also increasing. In response, listed companies are progressing with disclosure, through integrated reports, sustainability reports, environment reports, etc., as well as through more fragmented media such as company websites.

However, there is research suggesting that most investors see the current level of ESG disclosure as inadequate. A survey by the Life Insurance Association of Japan (below) showed that while 28% of companies surveyed thought that the current level of corporate ESG disclosure was adequate, the figure among investors was only 1%[16].

In the same survey[17], the proportion of companies who responded that they "Understand" or "Understand to some extent" investors' information needs was almost 70%, although almost 30% replied that they "Don't really understand" or "Don't understand" investor needs at all.

Companies can understand an investor's needs and ways of thinking through dialogue with that investor, but in reality, investors are diverse and it will be hard to understand everything just through dialogue. For many listed companies, the gap in understanding between themselves and investors can be made smaller by understanding the many existing frameworks, which reflect the voices of investors.

Is the current level of corporate ESG disclosure adequate?



Source: The Life Insurance Association of Japan (2019) "Initiatives by Life Insurers to Reinvigorate the Equity Market and Achieve a Sustainable Society through Asset Management" (edited)

[16] The Life Insurance Association of Japan (2019) "Initiatives by Life Insurers to Reinvigorate the Equity Market and Achieve a Sustainable Society through Asset Management"
〈https://www.seiho.or.jp/info/news/2019/pdf/20190419_3-5.pdf〉

[17] The Life Insurance Association of Japan (2019) "Initiatives by Life Insurers to Reinvigorate the Equity Market and Achieve a Sustainable Society through Asset Management" (Japanese only)
〈https://www.seiho.or.jp/info/news/2019/pdf/20190419_3-all.pdf〉

Inset 1.5: A letter to the world's CEOs from BlackRock

Every year Larry Fink, CEO of the world's biggest institutional asset manager BlackRock, sends a letter addressed to the world's CEOs. This letter has mentioned sustainability since 2016, and in 2020, entitled "A Fundamental Reshaping of Finance", it warned that climate change is a financial risk that could shake the stability of economic growth and the financial system, and called for governments, companies and shareholders to work together to fight it.

The 2020 letter also asked companies for disclosure based on the SASB Standards and the TCFD Recommendations, stressing that companies need to disclose so that investors can ascertain whether they are properly managing sustainability risks and opportunities.

Larry Fink's letter to CEOs is available on the BlackRock website.

https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter

ESG in the Corporate Governance Code

The Japanese Corporate Governance Code sets out the main principles of effective corporate governance. It is expected that implementing effective corporate governance will contribute to the sustainable growth and corporate value creation of each company through self-motivated actions, as well as improving these things further through dialogue with investors.

The Code looks in general from the point of view of investors and other stakeholders, so although the General Principles deal with G (governance) as a framework for making transparent and fair but also fast and decisive decisions, the Code also mentions E (environment) and S (social) issues in the context of good governance. Principle 2.3 states that "Companies should take appropriate measures to address sustainability issues, including social and environmental matters", while supplementary principle 2.3.1 adds, "With the recognition that dealing with sustainability issues is an important element of risk management, the board should take appropriate actions to this end. Given the increasing demand and interest with respect to sustainability issues in recent years, the board should consider addressing these matters positively and proactively."

On the theme of ESG disclosure, the Notes for General Principle 3 state that "while the quantitative part of financial statements of Japanese companies conform to a standard format and therefore excel with respect to comparability, qualitative and non-financial information, such as financial standing, business strategies, risks and ESG (environmental, social and governance) matters,

is often boiler-plate and lacking in detail, therefore less valuable. The board should actively commit to ensure that disclosed information, including non-financial information, is as valuable and useful as possible."

ESG issues and your business

As previously discussed, there is a growing number of investors who acknowledge that a company's actions on ESG issues affect its sustainability and corporate value. Use of ESG information in the investment industry is also progressing. The Ministry of Economy, Trade and Industry's Guidance for Collaborative Value Creation discusses ESG as a part of a company's sustainability and sustainable growth, which joins together its values, business model, strategy etc. – in this way, ESG issues are not only relevant to one part of a company's operations, but to the entire process of value creation. The next Step introduces processes that can be used when thinking about which ESG issues are most relevant to your company's business.

Step 2: Connecting ESG Issues to Strategy

As ESG issues are diverse and wide-ranging, working on every ESG issue that connects even lightly with a company's business would be a huge undertaking. As a result, it is important that in order to improve sustainability and aim for better corporate value, each company identifies the ESG issues which have strong links to their strategy and moves forward focusing on those. From an investor perspective, when evaluating a company's mid- to long-term prospects, it is useful if the ESG issues which the company has judged as important from a mid- to long-term corporate value creation and sustainability perspective, and the company's activities in response to those, are explained with reference to their link to corporate value.

There is no universally agreed system for identifying the important ESG issues to a company, but one suggested way to start is to look into what risks and opportunities ESG issues can provide in terms of the company's business model and strategy. This Step introduces some points to think about when looking into the connection between ESG issues and your company's business model/strategy, along with actual examples of how this can be done.

Section 1 (ESG and its impact on strategy) and Section 2 (Identifying what is "material") of this Step have many mutual links to each other in practice and there may be some elements which are hard to clearly separate. Consequently, companies should consider implementing the main points set out here in whatever order and with whatever processes work for them in particular depending on their circumstances.

Sections

2-1 ESG and its impact on strategy

2-2 Identifying what is “material”

- ”Materiality” and ESG
- Why materiality is important
- Making a material issues longlist
- Evaluating the importance of ESG issues
- Material issues and strategy

Related sections of existing frameworks

- SSE Model Guidance (2.2.1 Supporting corporate strategy; 2.3 Relevance and Materiality; 2.3.1 Identifying themes)
- GRI Standards (101: Foundation > 1. Reporting Principles > 1.1 Stakeholder Inclusiveness; 1.2 Sustainability Context; 1.3 Materiality; 2.3 Identifying material topics and their Boundaries)
- IIRC Framework (Part II – The Integrated Report > 3. Guiding Principles; 4. Content Elements)
- TCFD Recommendations (B Climate-Related Risks, Opportunities, and Financial Impacts; C Recommendations and Guidance > 3. Guidance for All Sectors > b. Strategy, c. Risk Management)
- WFE ESG Guidance (Guidelines for Report Preparation > Clarity of purpose/clear link to business value; Materiality)
- METI, Guidance for Collaborative Value Creation (2. Business Model; 3. Sustainability/Growth; 4. Strategy)
- SASB Standards (by sector)

2-1 ESG and its impact on strategy

ESG issues can have an impact on a company's business model or strategy as either, to put it broadly, a risk or an opportunity. (A risk, for example, could be that a new regulation stops you from providing a certain product or service. An opportunity could be that a newly developed technology enables you to break into a new market.) Taking this into account, the first step for considering which ESG issues could impact your company strategy is to analyse possible impacts on the company through the prism of risks and opportunities.

From the disclosure perspective, investors trying to judge corporate value will find it useful to have ESG issues which the company has identified as important introduced along with an explanation of what kind of initiatives on risk management and revenue-making opportunities the company has included in their strategy in relation to those issues. Ideally, disclosure should include information enabling investors to calculate financial returns, such as how cashflow will rise or fall in the future, how much the discount rate will change after risks are dealt with, or how much your asset composition or value, etc. will be impacted. However, even if this is difficult, qualitative information or any way you can explain the link to corporate value is important.

As company strategies will differ depending on size, sector, geography, and other things, the points to take into account when thinking about the impact of ESG issues on strategy will also differ from company to company. This section introduces some points based on actual cases of disclosure.

ESG and company values

Identify ESG issues that have an impact on your activities based around company values, such as the company philosophy or vision.

ESG and business models

Identify the connection between ESG issues and your business model from a corporate value creation perspective. Work out what kind of ESG issues will impact, and how they will impact, the factors that make up your business model, for example your place within the value chain, or the factors which differentiate you from the competition and the resources which enable those factors.

ESG and business/asset portfolios

Analyse the impact ESG issues could have on your individual businesses or assets and look into how these could be handled. For example, consider the impact a change in the regulatory environment could have on the operations or value of each asset you hold, and identify the necessary response.

ESG and operations/supply chains

Identify what kind of ESG issues could impact your operations from the standpoint of ensuring an uninterrupted supply of resources, etc., and analyse your entire supply chain to identify possible impacts in the mid to long term

and how these could be handled.

ESG and research development

Identify what kind of research development and human resources training you can put in place to maintain or strengthen your competitiveness in case of a large expected risk or opportunity stemming from ESG issues. When doing this, think about whether that kind of investment will be supported by investors and other stakeholders.

ESG and products/services

Identify whether any ESG risks or business opportunities could apply to your current products and/or services.

ESG and markets/customers

Consider the possibility that wider concern about ESG issues could cause shifts in the choices, values, and lifestyle, etc. of the markets and/or customers that you target. If this is the case, identify how this will affect your company and what you can do to handle those impacts.

Examples 2.1: How companies disclose the relationship between ESG issues and strategy

ESG and company values

Firm A: Global consumer goods manufacturer

Firm A is a consumer goods manufacturer with operations around the globe. Its purpose is "To make sustainable living commonplace", and under this it aims to deliver long-term growth and sustainable value creation. With the knowledge that growth and sustainability complement each other, it has created and disclosed a sustainability plan covering all aspects of the business and value chain and incorporating all brands and divisions. The three aims of the plan are: 1) Improving health and well-being, 2) Reducing environmental impact, and 3) Enhancing livelihoods, and for each one A has identified the business areas necessary for achievement. In addition, A has split the ways that sustainability is contributing to the business into a) more growth, b) less risk, c) lower cost, and d) more trust, and explains these with specific examples.

ESG and business/asset portfolios

Firm B: Global energy provider

Global energy provider B has built a business model which integrates the management of financial and non-financial risks and opportunities. Under this model, it has created a strategy to take the best opportunities arising from the transition to a low-carbon economy, and to achieve this, it has set a target to entirely decarbonise the energy it supplies by 2050, and has invested widely in wind farms and solar power plants across the world.

ESG and operations/supply chains

Firm C: Global electrical goods manufacturer

Firm C sells and supplies electrical goods globally and its supply chain is equally huge and wide-ranging, meaning that it takes supply chain management seriously. C carries out regular assessments of its suppliers, including their staff education programs, attitude towards human rights, and climate change activities, and works with them to ensure improvements where needed. If improvements are not made, it ends its relationship with that supplier. C discloses information on its supply chain policies and supplier assessments in a standalone annual report on supplier responsibility.

ESG and research development

Firm D: Global consumable goods manufacturer

Firm D is a food and drinks company with global operations. D believes that business benefits and positive societal impact must be mutually reinforcing, and that thinking about shared value in this way is in the long-term interests of all stakeholders. With this in mind, D has set a goal of making all food and drinks packaging recyclable, and as part of achieving this, has founded a research consortium along with other members of the industry with the goal of developing packaging made with 100% sustainable and renewable resources. The consortium is planning to build a factory capable of producing the packaging they develop.

ESG and products/services

Firm E: Global car manufacturer

Firm E is a car manufacturer with global reach. Under the belief that there is no future for cars unless the company responds to environmental issues such as climate change, in order to ensure sustainable development together with society, E has set itself a number of challenges to complete by 2030 and 2050. One of these is to reduce global average CO2 emissions from new vehicles by more than 35% by 2030 and 90% by 2050. To achieve this, E intends to hugely increase sales of electric and hybrid vehicles.

2-2 Identifying what is "material"

In the field of ESG investment, important ESG issues which impact a company's strategy or corporate value are referred to as "material". The process of identifying which issues are material is often called "materiality analysis" and many companies disclose this information publicly.

In many cases, companies use existing ESG disclosure frameworks and other things to make a list of the ESG issues that could possibly have an impact on their corporate value, and then narrow the list down by evaluating their importance in the context of, for example, their company values, business model, strategy, and impact on stakeholders. The IIRC Framework explains a similar process to this in section 3D, "Materiality", which is a good reference to use when providing information to shareholders and other stakeholders.

This section introduces some points to think about when identifying material issues. As materiality will differ from company to company, there is no set way to do this, but the points below are based on actual cases of disclosure and may be helpful during the process.

"Materiality" and ESG

The word "material" is a general term used to mean essential or vital, but it has a specific meaning in the context of financial information. The International Accounting Standards Board (IASB) states that "Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity [18]. Similarly, the Japanese Financial Services Agency (JFSA) writes in their Principles Regarding the Disclosure of Narrative Information that "The materiality of narrative information should be judged based on whether or not it is material to investors' investment decisions."[19]

Materiality is also an important concept in the field of ESG disclosure, and existing frameworks have set out their own definitions or ways of thinking about materiality based on their own policies. In Japan, the Guidance for Collaborative Value Creation writes that "For investors, it is important to understand how companies understand the materiality of ESG factors to the sustainability of their business models."

Overseas, the IIRC, which mostly relates to disclosure aimed at investors, defines material information as "matters that substantively affect the organization's ability to create value over the short, medium and long term". The GRI Standards, which think more about information

[18] IFRS website "IASB clarifies its definition of 'material'" <https://www.ifrs.org/news-and-events/2018/10/iasb-clarifies-its-definition-of-material/>

[19] Japan Financial Services Agency (2019) "Principles Regarding the Disclosure of Narrative Information" <https://www.fsa.go.jp/en/news/2019/20190606-3/01.pdf>

aimed at multiple stakeholders including investors, defines it as "topics that reflect the reporting organization's significant economic, environmental, and social impacts; or substantively influence the assessments and decisions of stakeholders."

It is important that each company thinks about these different definitions of materiality and decides on one to use depending on the specific aims, audience, or other circumstances of their disclosure.

Why materiality is important

The range of ESG issues that can relate to business operations is huge, but what is relevant to each company differs depending on things such as their industry, geography, business model, strategy, and business environment. While it can be said that many issues relating to G (governance) are common to all companies, E (environment) and S (social) issues vary massively depending on the company or sector.

In order to efficiently allocate limited resources to maximising the sustainability of your business operations in order to improve corporate value, it is important to identify which issues are material, i.e. have a strong connection to your corporate value, and decide on measures to respond to these in particular.

From a disclosure perspective, investors trying to evaluate a company's mid- to long-term corporate value or the sustainability of its operations will find it very useful to have disclosure of which ESG issues said company has judged as material to its corporate value, along with information on the company's activities in response to these. For example, it is useful to explain which measures in response to ESG issues will be important to ensure the company meets its mid- to long-term financial targets (such as ROE or future cashflow).

Example 2.2: Materiality analysis from Japanese financial firm "F"

Firm F's mission is "To contribute to the development of a vibrant society and help secure a sound future for the planet, by enabling safety and peace of mind through the global insurance and financial services business." Under this mission, F identifies social issues to which it will have to respond in the mid to long term, taking into account the possibility of drastic societal change. Then, in order to contribute to solving those issues and create a "resilient and sustainable society" by 2030, using the SDGs as leading marks, the company picks out priority issues which it will work on as challenges for Creating Shared Value (CSV, for both society and the company).

Step 1: Analysis of social issues

The company identifies social issues (below) to which it can make a significant contribution, based on input from stakeholders (customers, shareholders, business partners, the environment, local society, international society, employees, and agencies), as well as international frameworks and their goals.

1. Diversified/large-scale accidents and/or disasters	2. Global environment approaches the limit	3. Mounting burden of nursing/medical care due to aging population	4. Economic slowdown by widening inequality

Step 2: Identification of priority issues

The company identifies priority issues (for CSV) by analysing the social issues based on whether the company can make a significant contribution and whether they have a major impact on the company's long-term growth, for each area of economy, society, and organisational governance.

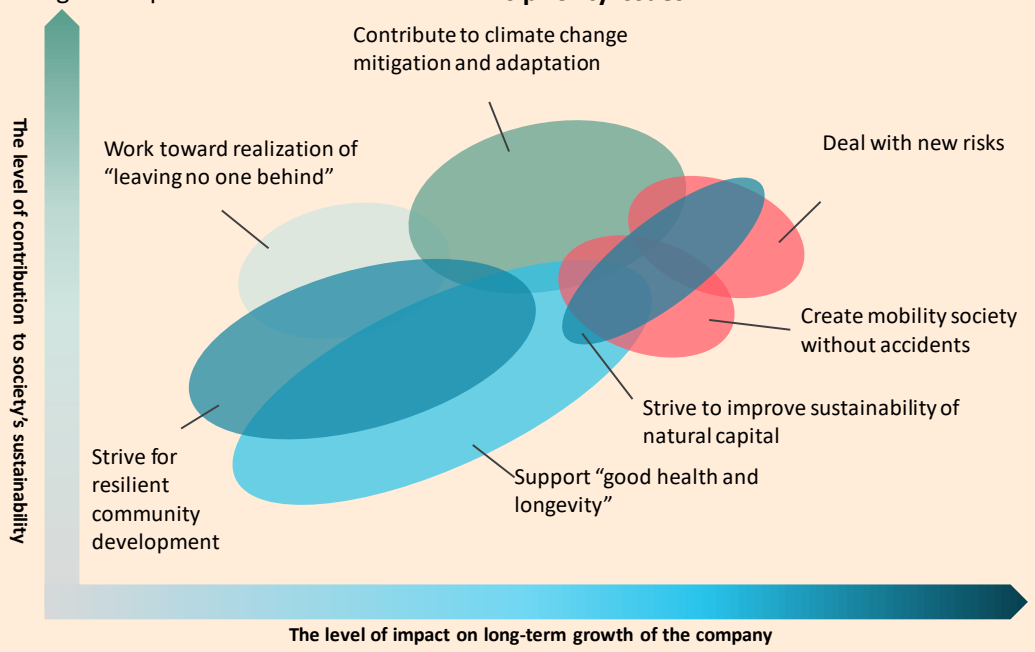
Step 3: Identifying core initiatives to underpin priority issues

The company decides on core initiatives to respond to each priority issue.

Step 4: Reporting to the management team

The identified core initiatives are reported to the management team and reflected in the medium-term management plan.

Firm F's priority issues



Example 2.3: Materiality analysis from Japanese pharmaceutical firm "G"

Firm G has concluded that in order to sustainably maximise corporate value for the satisfaction of all stakeholders, it is efficient to focus on long-term investors as they are the beneficiaries of residual income. With the long-term interests of all stakeholders taken into account, G identifies material issues with the belief that finding which issues relate to long-term investor interests and prioritising action on these is a fast-track way to maximise corporate value.

Process 1: Identification of issues

G picks out a range of issues with reference to various frameworks (SASB, GRI, SDGs), communication with stakeholders, and metrics used for evaluation of socially responsible investment.

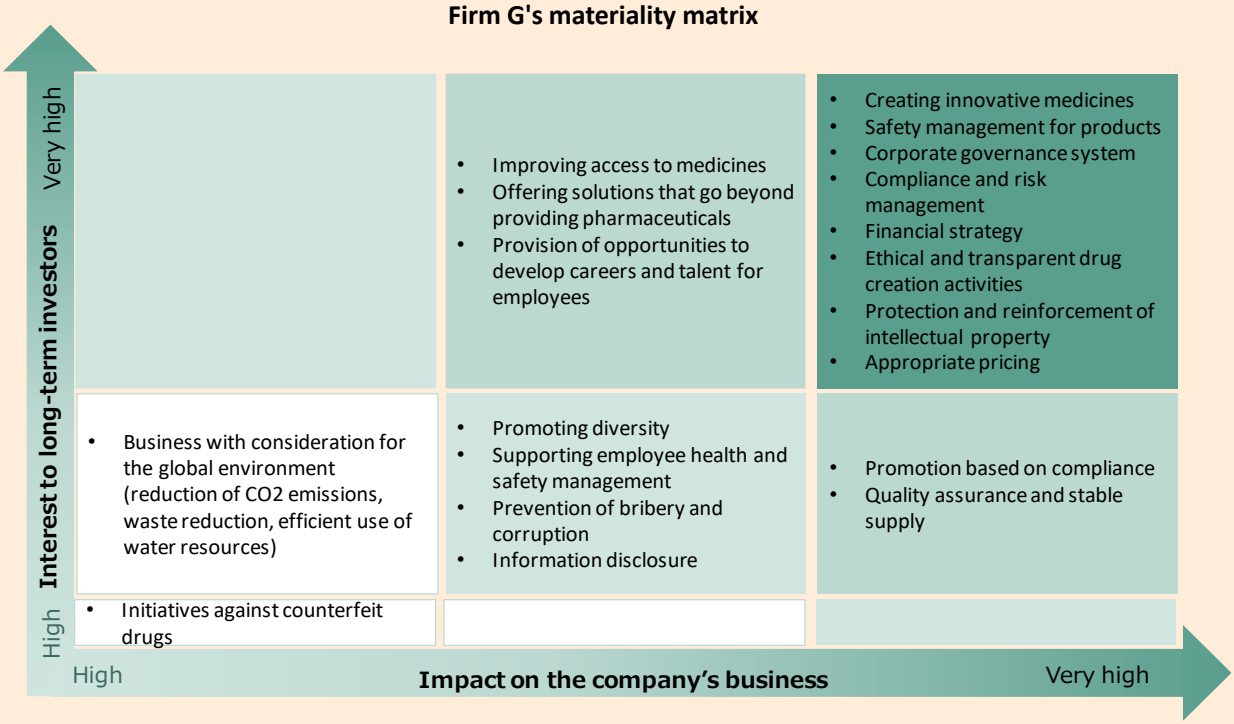
Process 2: Prioritisation of issues and creation of materiality matrix

The company then creates a matrix (below) to decide on the order of priority of each issue depending on its "impact on the company's business" including impact on finances and the corporate philosophy, and its "interest to long-term investors" including its financial reporting, opportunities to create innovation, and the impact of legal restrictions, etc.

Process 3: Reviews and updates

The company carries out reviews and updates where needed, taking into consideration the progress of activity in response to the issues and changes in the business environment.

Firm G's materiality matrix



Making a material issues longlist

If we look at existing company disclosure on materiality, there are a number of examples of companies identifying material issues by first making a wide-ranging list of ESG issues from international disclosure frameworks and analysis of their business environment, before narrowing the list down to the most relevant material issues by evaluating each issue's importance.

If resources are limited and you find it difficult to make a longlist of ESG issues from scratch, the below stages of the process are not essential, but creating a list of possible issues using existing frameworks can enable you to find material issues which may otherwise have been missed with discussions and viewpoints limited to within the company or to certain timeframes.

Analysis of business environment

A good first stage of looking into what ESG issues may affect your corporate value or sustainability is to analyse long-term changes in the environment in which you do business. Useful references for this can be found in reports and other publications from governments, international organisations, think tanks and the like, both inside and outside of Japan, such as the World Economic Forum's publicly available Global Risks Report[20].

Using existing frameworks

As preparation for identifying material ESG issues, the companies in the previous pages' examples made longlists of possible material issues partly by referring to existing frameworks. Two examples of frameworks which can be useful in this way are the SASB Standards and the GRI Standards.

In addition, more companies have recently begun referring to the 17 Goals and 169 Targets that make up the SDGs in their disclosures.

Using ESG rating agency surveys

Companies which research on ESG issues and provide company ESG ratings (see page 43) are referred to as ESG ratings agencies. In the process of providing these ratings, such agencies carry out surveys on listed companies which focus on specific disclosure contents and specific ESG activities chosen from the full range of ESG issues depending on investor interest. Although the surveys do not target all companies and not all research contents or methods are disclosed, agencies edit their chosen issues year-to-year depending on external changes and investor movements, so they can be used as a reference while narrowing down your material issues.

Dialogue with stakeholders

Candidates for ESG issues can also be found by conducting interviews with stakeholders (investors, employees, trading partners, customers, experts, etc.) to find out what is important to them and what they expect of your company.

[20] The Global Risks Report can be accessed from the World Economic Forum website at <https://jp.weforum.org/reports>

The sector-based approach

The material issues longlist will as a rule differ depending on business models and lines of business, etc., but for analysis of the business environment, which is particularly important to ESG, it can be said that many issues will be common to a sector. The sector-based approach is also important since many investors will be deciding on investments by comparing companies from one sector across the globe.

Some existing frameworks provide lists of material issues which are common, to an extent, to specific sectors. For example, SASB has set specific disclosure points and targets for 77 separate sectors to encourage disclosure useful for investment decisions.

If your company finds it difficult to identify material issues by making a longlist from scratch, one alternative could be to use an existing sector-based list as a foundation.

Evaluating the importance of ESG issues

After a material issues longlist is created, it will need to be narrowed down by evaluating how each issue links to corporate value. There is no set way to evaluate the importance of each issue, but below are some points to consider based on actual cases of disclosure.

Setting evaluation factors

Once you have made a longlist, you will need to find some kind of method of evaluating each issue's importance in order to find which are material. In the previous pages' examples, companies evaluated each issue using factors such as "Importance to the company" and "Importance to stakeholders".

Evaluating issues in practice

Once you have chosen factors, you will then need to evaluate the importance of each issue using those factors. Below are some points to consider when doing this.

1. Importance to the company

The importance of an issue to a company is essentially how it links to the company's sustainability and mid- to long-term corporate value, but to judge this, many companies identify the issue's connection to their company philosophy or values, and analyse what kind of risks it poses/opportunities it presents to the company's strategy or each business, as well as the impact of those and how often they could occur.

2. Importance to stakeholders

The importance of an issue to a company's stakeholders can be used as an evaluation factor, but only if the company has decided who its stakeholders are. For example, when thinking from a perspective of linking ESG activities to mid- to long-term corporate value creation, your main stakeholders may be long-term investors, but may also include customers, employees, possibly even international organisations, NGOs or the local community.

There are cases of companies sending out surveys to their stakeholders in order to evaluate or measure what is important to them, and also companies conducting interviews with experts in ESG issues who can speak on behalf of multiple stakeholders.

Timeframes

There may be ESG issues which present risks and opportunities to a company in different ways depending on the timeframe. For example, thinking about the effects of climate change, it is likely that the impact on your company and the actions you take in response will be different in 20-30 years as opposed to 2-3 years. As a result, when evaluating the importance of ESG issues, it is important to think about what timeframe(s) to focus on.

Involvement from the top

Companies may wish for the company's executive officers and/or the Board of Directors, etc. to be involved in making the final decisions over what is material.

Material issues and strategy

In order for a company's responses to material issues to lead to improved corporate value, it is important that the chosen material issues are reflected in company strategy or strategies for individual business lines. In addition, when it comes to moving forward with ESG activities, it is important to create a policy and/or action plan to guide these activities in line with those strategies.

Reflecting material issues in company strategy

In order for the material issues you have identified to contribute to corporate value, it is important to reflect them in your company strategy or objectives and work from there. Then, it is important for investors that this is explained in an integrated report or other material. There are examples of companies using their integrated report to explain the connection between material issues and their mid-term management plan or how the company intends to look in the mid to long term, and even companies referring to materiality in their top message.

Creating an ESG policy/action plan

When looking to move forward with ESG activities in response to your chosen material issues, it is important to create a policy and/or action plan to guide those activities. This policy/action plan can be developed based on the company's business environment, its ideal future vision and how it plans to achieve that, and available resources.

Step 3: Oversight & Implementation

In order for a company to link its chosen material ESG issues with corporate value creation, it is important that activity in response to those issues is carried out as an organisation, and that said organisation has a suitable and well-functioning governance system in place. Furthermore, by disclosing information about the governance system, companies can enable investors to understand how the activities that formed the basis of their investment decisions are actually contributing to the company's sustainability and corporate value creation.

Sections

3-1 ESG in the decision-making process

- Commitment from the top
- Governance

3-2 Setting metrics and targets

- Setting metrics
- Setting targets
- Carrying out a PDCA

Related sections of existing frameworks

- SSE Model Guidance (2.1 Responsibility and Oversight; 2.3.2 Adopting relevant performance indicators; 2.5.1 Robust internal ESG data collection and management processes)
- GRI Standards (101: Foundation; 102: General Disclosures; 103: Management Approach)
- IIRC Framework (Part II – The Integrated Report > 4. Content Elements)
- TCFD Recommendations (C Recommendations and Guidance > 3. Guidance for All Sectors > a. Governance; d. Metrics and Targets)
- WFE ESG Guidance (Guidelines for report preparation > Governance/Responsibility and oversight)
- METI, Guidance for Collaborative Value Creation (5. Performance and Key Performance Indicators (KPIs); 6. Governance)
- SASB Standards (by sector)

3-1 ESG in the decision-making process

To begin activities in response to chosen material ESG issues and connect these to corporate value creation, it is important to incorporate them into the structure of the company's decision-making process as you would with other management issues. To do this, commitment from the top of the organisation and a suitable governance system are essential.

Commitment from the top

In order to respond to ESG issues from the perspective of corporate value creation, it is important that the top-level management of your organisation is involved and takes responsibility. To show that management have taken responsibility in a way useful to investors, you could disclose for example a map of allocations of responsibility for ESG issues, the process for sharing information internally with management, and/or how you monitor ESG issues on an ongoing basis[21].

Governance

Each company should put in place a governance system for ESG issues which fits to that company, based on existing management/governance systems. Most importantly, however, identification of and discussions on ESG issues should, like other governance issues, take place within the decision-making and oversight function, i.e. the board of directors, and include outside directors.

If the company has a separate executive board in charge of day-to-day operations below the board of director or top management level, including ESG issues in this board's responsibilities in the same way as other issues will further link ESG issues to the company strategy.

The function of the board of directors

The board of directors is responsible for oversight of whether the response to ESG issues is being suitably carried out, and whether this is leading to corporate value creation. For this to happen, it is important that there is a process for reporting to the board, and that ESG issues are included as part of discussions on strategy, risk management, and business planning, etc. The board should also monitor and oversee progress towards targets related to ESG activities.

Implementation (allocating a responsible department)

For implementation of your company's response to ESG issues, to support the above governance system, you could either allocate a responsible department within the existing structure, or create a new designated unit which can co-ordinate ESG issues across departments. In either case, it is important that

[21] One of TCFD's Recommended Disclosures is to "Describe management's role in assessing and managing climate-related risks and opportunities." (The TCFD Recommendations: <https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf>)

the response to ESG issues is not carried out independently by the responsible department, but by the entire company. The responsible department could have the following responsibilities:

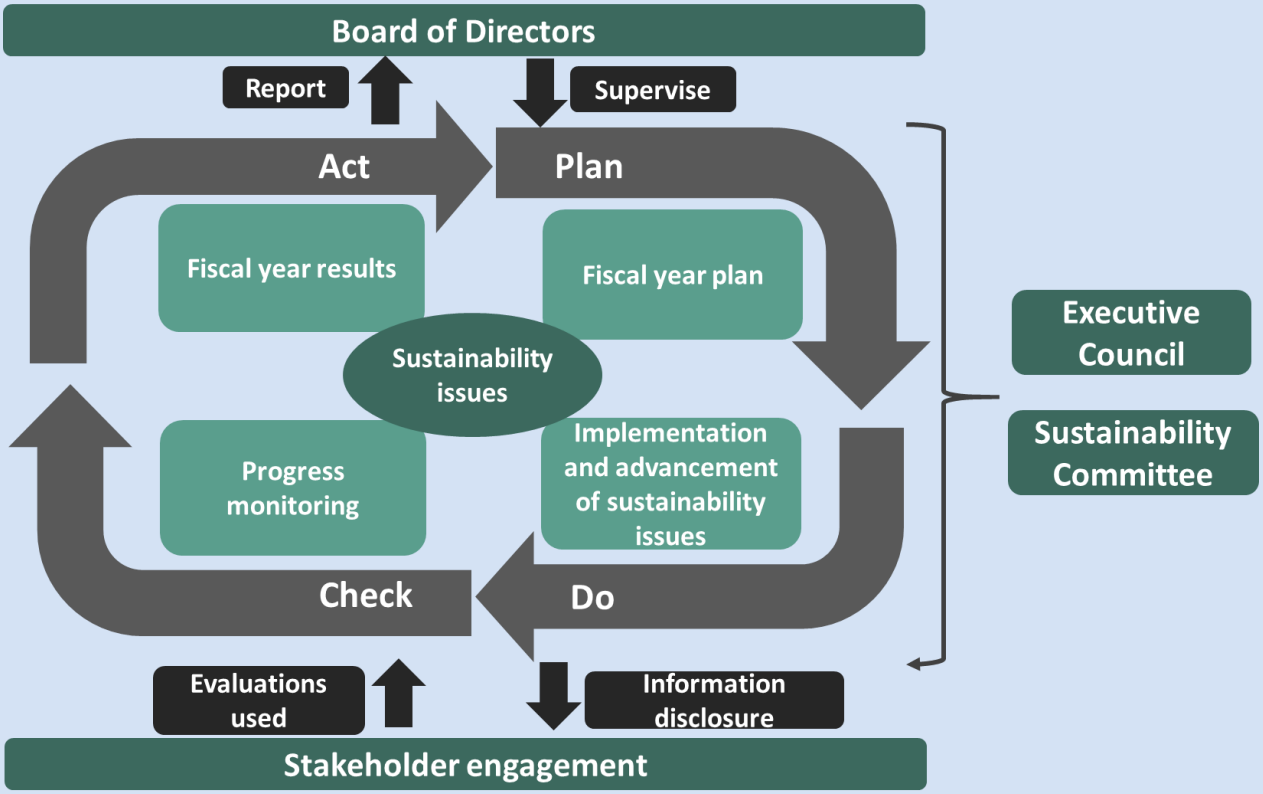
- Gathering/understanding information on changes in the business environment: Activity in response to ESG issues should be carried out with a mid- to long-term perspective, but it also can be expected that the issues themselves or their importance will shift over time in response to external changes. The responsible department for ESG will need to gather and understand information on these changes so that your company's material issues can be reviewed regularly.
- Co-ordinating across departments: As activity in response to ESG issues does not always fall neatly within the responsibilities of existing departments, often requiring company-wide co-operation, the responsible department for ESG can be expected to help the smooth running of these projects by co-ordinating across departments.
- Reporting to the board of directors/executive boards: The responsible department for ESG should report to the board of directors and/or other executive boards on analysis of ESG issues and progress of ESG activities, etc.
- External engagement: The responsible department for ESG should respond to investor enquiries on ESG and surveys from ESG ratings agencies and should communicate with international organisations, NGOs and others as necessary.
- Spreading awareness within the company: To move forward on ESG activities as an organisation, it is important that your material ESG issues and their connection to corporate value and strategy, etc. is understood throughout the company. The responsible department for ESG could be in charge of encouraging awareness through creating opportunities for debate or learning for all employees, starting maybe with just general ESG issues and the external environment.

Example 3.1: The sustainability management structure of Japanese manufacturing firm "H"

Firm H aims to contribute to the creation of a sustainable society and enhance corporate value, by solving social issues through its business activities under the company philosophy.

The company identifies material issues using two factors: social issues that need to be solved within the company's business areas, and issues that meet the expectations of stakeholders by strengthening business foundations. It then sets targets related to these issues. In addition, the company has set up a company-wide management structure in order to achieve these targets, and has made steady progress in solving individual issues through Sustainability Promotion Committee and Executive Council discussions, as well as engagement activities in response to stakeholder evaluations. The Board of Directors receives reports from operating divisions, enabling it to supervise and oversee all sustainability-related activity.

The sustainability management structure of firm H



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3-2 Setting metrics and targets

To make sure that activities in response to material issues actually lead to corporate value creation, where possible it is useful to set suitable metrics to measure progress by in line with the company's strategy or ESG policy/action plan. In this case, suitable metrics should be set based on where and in what way the chosen material issues will affect the company's business. It is also good to set targets where possible.

However, for those just starting out with ESG disclosure, the setting of metrics and targets is perhaps more difficult to implement than the other processes in this Handbook. In this case, it may be advisable to begin disclosing the other points with a view to finding suitable metrics and targets later on through dialogue with investors, etc.

Setting metrics

When beginning activities in response to material issues, it is useful to make clear your ideal future vision for the company and how you intend to achieve it, and set metrics for each issue to manage your progress. These metrics may be qualitative or quantitative, but either way they should be suitable for your company based on your chosen material issues. While these metrics can be unique to your company, it is also possible to use metrics set out in existing frameworks, as these take into account the views of shareholders and enable easier comparison between companies. For example, SASB (p39), GRI (p40) and the World Federation of Exchanges (WFE, the below table) have all published possible metrics.

Setting targets

It is also recommended to add targets to these metrics where suitable and disclose them. When deciding on these, it is important to think about what you need to aim for/achieve in the short and mid term in order to achieve your long-term vision or goals. It is also useful when deciding targets to involve the businesses or departments which will actually carry out the related activities.

In terms of how to set specific targets, each company should use a process suitable for their circumstances, but in general there are two possible processes:

- Calculate future predictions by looking at past achievements and set targets based on those.
- Look at targets set by domestic or overseas organisations or governments on environmental and social issues and set targets in reference to those.

The second of these is referred to as "backcasting" and is endorsed by the TCFD Recommendations (for climate change targets) and others.

Carrying out a PDCA

As well as incorporating chosen material issues into strategy and activities, companies should make sure that each project is properly moving forward by implementing a PDCA (plan-do-check-act) cycle. Like for other management issues, a PDCA will involve evaluations of the progress of a project and progress towards related metrics and targets, and if problems are found, improvements to the project and reviews of the metrics and targets. In the case of material ESG issues, many companies also take into account changes in the external environment and review the material issues and/or their importance accordingly.

WFE's ESG metrics

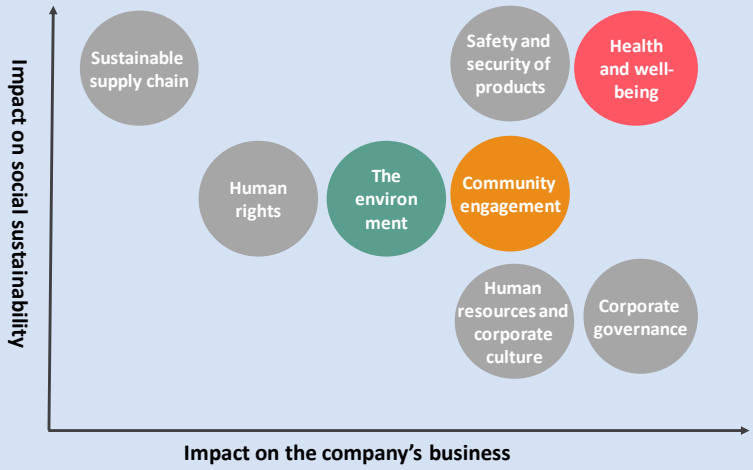
Environmental	Social	Governance
• GHG emissions • Emissions intensity • Energy usage • Energy intensity • Energy mix • Water usage • Environmental operations • Environmental oversight • Climate risk mitigation	• CEO pay ratio • Gender pay ratio • Employee turnover • Gender diversity • Temporary worker ratio • Non-discrimination • Injury rate • Global health & safety • Child & forced labour • Human rights	• Board diversity • Board independence • Incentivised pay • Collective bargaining • Supplier code of conduct • Ethics & anti-corruption • Data privacy • Sustainability reporting • Disclosure practices • External assurance

Based on WFE (2018) "WFE ESG Revised Metrics June 2018". See page 67-68 for more details

Example 3.2: Materiality and targets of Japanese consumable goods maker "I"

Firm I has identified "Health and well-being", "Community engagement" and "The environment" as key social issues among the social issues that affect the company. To face these issues, the company has formulated a Purpose (a long-term management vision) to guide how it creates shared value with society and promotes sustainable growth. It has then created and disclosed non-financial targets necessary to achieve its ideal future vision, based on this Purpose..

Firm I's material issues, commitments and targets



Health and well-being	Community engagement	The environment
Raise the number of healthy people, lower the number of sick people, and contribute to the people who are involved in healthcare	Create more opportunities for customers to spend time with their families and friends, and develop the communities within our supply chain	Realise a society based on 100% resource circulation by 2050

Issue	Commitment	Approach	Target
Health and well-being	Supporting self-care for healthy people and people with pre-disease	1. Develop and expand sales of no-sugar products and products with scientifically proven health benefits 2. Continue to create new value in ingredients with health benefits	1. Rate of sales increase: 115% compared with 2015 2. Number of countries capable of purchasing: Five countries (roughly 650 million people)
	Evolution in medical treatment	Strengthen our drug discovery foundation to develop and provide new drugs globally based on the strengths of R&D and production capability acquired through developing and providing biologics	Number of new drugs released to market in multiple regions and number of countries: Three or more products launched in over 50 countries
Community Engagement	Contributing to community vitalisation	Create and increase opportunities that bring people together at dining tables, recreational activities, seasonal events, and sports and music events with our products	Number of products and services that create opportunities to bring people together (target under consideration)
	More sustainable production of raw materials	Take a long-term perspective to enhance the value of raw materials and support production area and contracted firming toward achieving sustainable procurement and revitalisation of production areas 1. Amount of Japanese ingredients procured 2. Contracted firming ratio 3. Number of small-scale farmers supported for acquisition of Rain Forest Alliance certification	1. 100 tons in 2027 2. 10% in 2027 3. 10,000 farmers in 2025
The Environment	Actions regarding climate change	Introduce renewable energy and promote energy conservation	Reduction ratio of GHG emissions: 30% in 2030 compared with 2015
	Actions regarding containers and packaging	Strive to maintain the 3Rs and resource circulation for containers and packaging	Conversion rate of PET bottle resin to recycled resin: 50% in 2027

Metrics recommended by existing frameworks -1-

Sustainability Accounting Standards Board (SASB) (see pages 60-61 for more details on SASB)

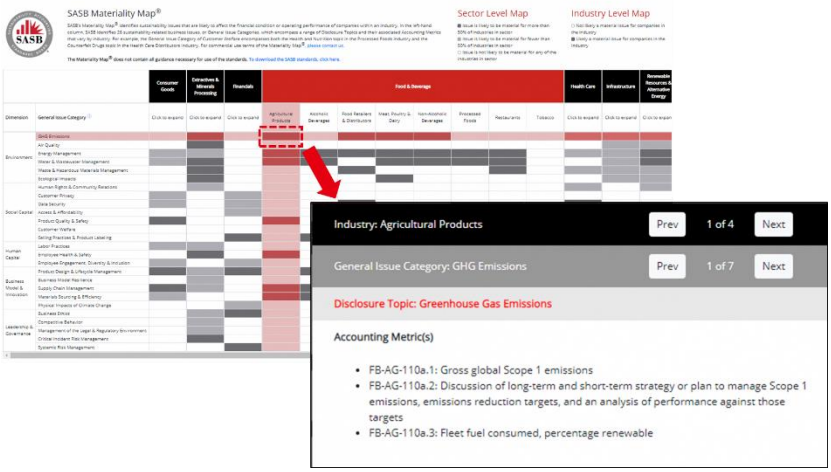
With the aim of contributing to the decision-making process of mid- to long-term focused investors, SASB has set disclosure standards for ESG issues that it identifies as reasonably likely to have material impacts on companies in an industry, and published standards for 77 industries within 11 sectors in November 2018. The SASB Standards are available for download from the website below (currently available only in English).
https://www.sasb.org/standards-overview/download-current-standards/

Intended to help analyse a company's sustainability, the SASB Standards are based on 26 "General Issue Categories" organised under five "Dimensions", as shown below.

Dimension	Environment	Social Capital	Human Capital	Business Model & Innovation	Leadership & Governance
General Issue Category	GHG emissions Air quality Energy management Water & wastewater management Waste & hazardous materials management Ecological impacts	Human rights & community relations Customer privacy Data security Access & affordability Product quality & safety Customer welfare Selling practices & product labeling	Labour practices Employee health & safety Employee engagement, diversity & inclusion	Product design & lifecycle management Business model resilience Supply chain management Materials sourcing & efficiency Physical impacts of climate change	Business ethics Competitive behaviour Management of the legal & regulatory environment Critical incident risk management Systemic risk management

Disclosure Topics and Accounting Metrics are then set for each of the General Issues judged to be material for each particular industry, and set out in detail in the Standards. Disclosure Topics and Accounting Metrics for each sector/industry can also be found in the SASB Materiality Map, which is available on the website: https://materiality.sasb.org/.

Disclosure Topics and Accounting Metrics as shown in the SASB Materiality Map



Metrics recommended by existing frameworks -2-

Global Reporting Initiative (GRI) (see pages 65-66 for more details on GRI)

GRI created its Standards including specific data points for disclosure as “the global best practice for reporting on a range of economic, environmental and social impacts”. The Standards are available from the below website, in both English and Japanese.
https://www.globalreporting.org/standards/gri-standards-download-center/

As listed below, the GRI Standards are made up of "Universal Standards" (101, 102, and 103) and "Topic-specific Standards" (200 series, 300 series, and 400 series). Issues for creating metrics are set out in each topic-specific series.

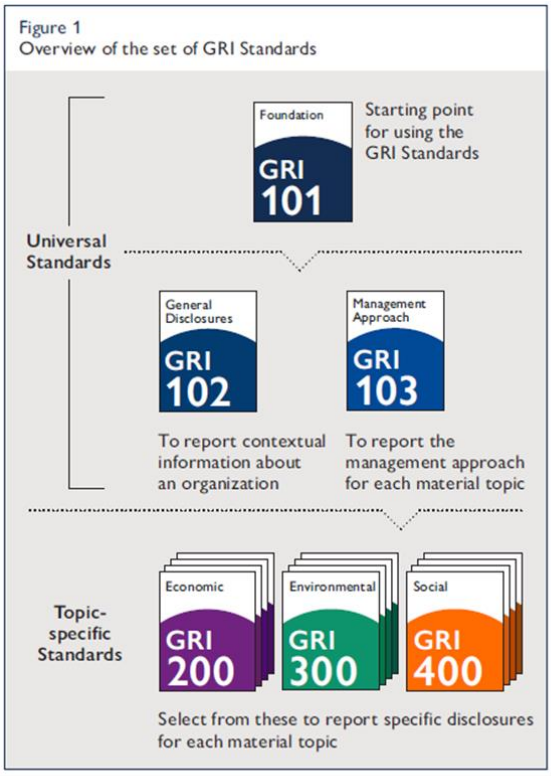
-GRI 101: Foundation - a guide to how to use the GRI Standards

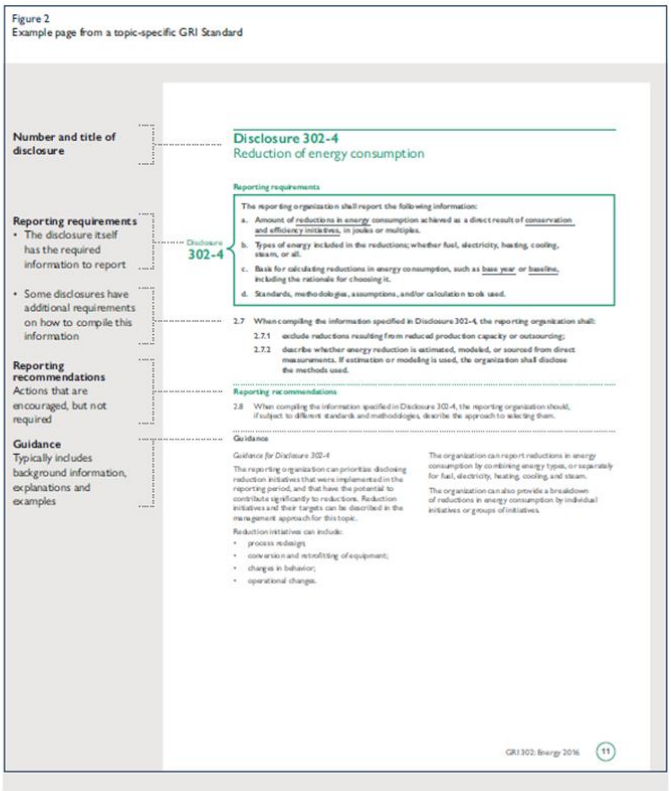
-GRI 102: General Disclosures - reporting an organisation's relevant contextual information

-GRI 103: Management Approach - reporting how material topics are managed

-GRI 200, 300, 400 series – data points for reporting information on an organisation's economic, environmental, and social impact.

Overview of the GRI Standards and an example page from a topic-specific GRI Standard





Source: GRI (2016) "GRI Standards"

Step 4: Information Disclosure and Engagement

When disclosing risks and opportunities stemming from a company's material ESG issues, it is important to disclose their relationship to strategy as well as corporate value, the oversight and implementation structures put in place to support this, and the progress of ESG activities. This will help investors to evaluate the company's mid- to long-term corporate value. In addition, carrying out engagement with investors based on this disclosed information will lead to deeper understanding from both sides, and help to move forward activities aimed at improving mid- to long-term corporate value.

Sections

4-1 Organising disclosure contents

- The link to corporate value
- Investor information sources

4-2 Using existing frameworks

- Information disclosure frameworks

4-3 Further points for consideration

- Platforms for disclosure
- English disclosure
- Third-party assurance of ESG data

4-4 Two-way engagement with investors

- ”Purposeful dialogue”
- Other types of engagement

Related sections of existing frameworks

- SSE Model Guidance (2.4 Accessibility, 2.5.2 Engaging for continuous improvement, 2.5.3 Assessment and assurance)
- GRI Standards (101: Foundation; 102: General Disclosures; 103: Management Approach)
- IIRC Framework (Part II – The Integrated Report > 3. Guiding Principles; 4. Content Elements)
- TCFD Recommendations (C Recommendations and Guidance > 1. Overview of Recommendations and Guidance; 2. Implementing the Recommendations)
- WFE ESG Guidance (Guidelines for report preparation > Quality & frequency of reporting)
- METI, Guidance for Collaborative Value Creation
- SASB Standards (by sector)

4-1 Organising disclosure contents

The link to corporate value

When aiming for disclosure which is useful for investors in evaluating your company's mid- to long-term corporate value, it will be necessary to include information on the risks and opportunities stemming from your chosen material issues, and paint a clear picture of how these link to strategy, governance systems, targets, etc. and ultimately corporate value overall.

One good reference material for this is the Ministry of Economy, Trade and Industry's Guidance for Collaborative Value Creation, published in 2017. The Guidance provides principles for communicating a company's values, business model, strategy, and governance, etc. to investors in an integrated manner.

The specific information you include will depend on things like the company's circumstances and who will be using the information, but as a general rule for disclosure aimed at investors, it is best to disclose information on the below points while taking into account their link to corporate value, as discussed in Steps 2 and 3.

- The link between ESG issues and strategy
- Material ESG issues and how they were identified
- Governance systems and commitment from the top
- Metrics and targets

If you would like to obtain a better picture of what good ESG disclosure can look like in practice, companies like the Government Pension Investment Fund (GPIF)[22] and Nikkei, Inc.[23] release lists of integrated reports which have been well-received by investors.

[22] From 2018, GPIF has published "Excellent Integrated Reports and Most-improved Integrated Reports selected by GPIF's asset managers entrusted with domestic equity investment". The 2020 winners can be seen on the below link.
<https://www.gpif.go.jp/en/investment/20200319_excellent_and_most-improved_integrated_reports_2019.pdf>

[23] Nikkei, Inc. has published the Nikkei Annual Report Awards since 1998 (Japanese only).
<http://adnet.nikkei.co.jp/a/ara/>

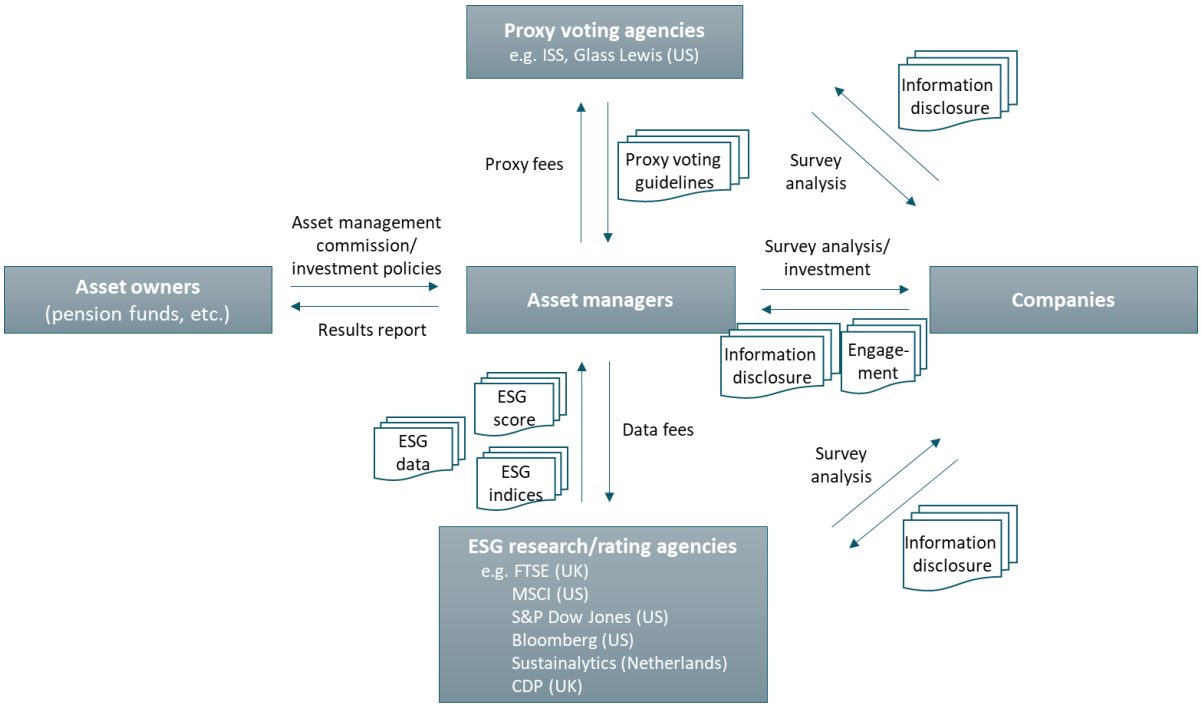
Investor information sources

So what kind of sources do investors actually use to gather information?

Asset managers, who are contracted by asset owners such as pension funds to manage their assets in practice, gather information mainly from three routes:

1. Directly from companies through disclosure and engagement.
2. Buying ESG data, scores, or indices etc. from information vendors or ESG ratings agencies. Vendors and ratings agencies calculate data and ESG scores from information collected both from company disclosures and surveys sent directly to each company.
3. For the purpose of executing voting rights, from information sent from companies in and with annual meeting notices, and sometimes data from proxy voting firms, in addition to the asset manager's own voting policies and information.

Investor information sources



When thinking about what ESG information to disclose and how to disclose it, it is important to understand who will be using the information and how. Also, if you receive surveys or feedback forms from ESG ratings agencies, looking at the topics included in them may help you see things from an investor perspective.

Inset 4.1: Disclosing quantitative data

Some investors use various types of quantitative ESG data in their investment decisions. Quantitative data includes, for example, greenhouse gas emissions, energy usage, or statistics on employee diversity.

One example of investors using data on greenhouse gas emissions is in Europe, where some pension funds and other investors have committed to make the carbon emissions from their investment portfolio net zero by 2050, and are therefore using investee companies' carbon emissions data for portfolio management.

In response to varied demands from investors and to make their disclosures clearer, some companies are now publishing quantitative data collectively in a data book or similar.

4-2 Using existing frameworks

Information disclosure frameworks

Many listed companies use existing information disclosure frameworks for their ESG disclosure, but when doing this, it is important to use the appropriate framework depending on who your disclosure is aimed at. Even just for disclosure aimed at investors, which this Handbook is focusing on, there are many existing frameworks which can be chosen depending on what kind of disclosure you are looking at.

A good summary of the existing frameworks can be found in "Study of ESG Information Disclosure"[24] commissioned by GPIF and created by Nissay Asset Management Corporation. Listed companies can use this information to gain an understanding of each framework's features and pick the best one(s) to use for their company.

Key backgrounds and features of existing frameworks and standards

Framework/Standard (Most recent revision year & country where based)	Key backgrounds and features
International Integrated Reporting Framework (2013/UK)	- Created a new form of corporate reporting, an integrated report that discloses both financial and non-financial information. - Information disclosure for investors. - Prepared based on principle-based approach without any predefined disclosure items and/or indicators. - Led by accounting organizations for the development.
GRI Standards (2018/Netherlands)	- The first edition was published in 2000, and this is one of ESG information disclosure frameworks/standards with the longest history in the world. - Information disclosure for multi-stakeholders including investors. - Disclosure items and indicators are defined for each of economic, environmental, and social aspects pursuant to rule-based approach (however, reporting companies are not required to disclose all items and indicators, but to disclose only items that are deemed material (important) by them. - An environmental NGO leads the establishment of GRI. - The structure changed in 2015 and the Global Sustainability Standards Board (GSSB) was established as an independent standard setting body.

[24] Government Pension Investment Fund (2019) "Study of ESG Information Disclosure" (Nissay Asset Management) <https://www.gpif.go.jp/en/investment/research_2019_full_EN.pdf>

SASB Standards (2018/US)	- Specific disclosure items and indicators are defined for each of 77 industries pursuant to rule-based approach (It defines that it is the company to make the final decision as to which topics are financially material.). - Information disclosure for investors. - At the development stage, they aimed at disclosure standards for US companies, but the status finally changed as disclosure standards for global companies. - For the purpose of development, practitioners were widely asked to participate in the standards consultation process, organized by sector/industry. Finally, more than 2,800 practitioners (businesses, financial analysts, consultants, etc.) were involved in the development. - SASB's governance structure includes an independent standards setting board (the SASB), along with the SASB Foundation Board which is responsible for overall administration.
TCFD Final Recommendations (2017/US)	- Recommended disclosure of climate-related financial information in the mainstream annual financial report, etc. - Disclosure of information for financial sector including investors (Note that requiring information disclosure by financial sector as well). - Basically, it is prepared based on the principle-based approach, but it clearly states that greenhouse gas emissions should be disclosed. - Sector-specific guidance has also been developed for certain sectors that are particularly relevant to climate change. - Developed by the task force established by the Financial Stability Board (FSB).
Guidance for Collaborative Value Creation (2017/Japan)	- Prepared by the Ministry of Economy, Trade and Industry as a guide to organize information to be communicated to investors (business philosophy, business model, strategy, and governance, etc.) in an integrated and systematic manner and to improve the quality of information disclosure and dialogue with investors. - Prepared based on principle-based approach without any predefined disclosure items and/or indicators.
Environmental Reporting Guidelines 2018 version (2018/Japan)	- Since the "Environmental Report Preparation Guidelines: How to Make Easy-to-Understand Environmental Reports" was formulated in 1997, the contents have been regularly revised - The Environmental Reporting Guideline 2018 added to its recommended disclosures information on the company's management approach regarding the shift to a sustainable economy. - It gives examples of disclosure indicators for each main environmental issue as a reference guide.
Annual Securities Report (2019/Japan)	- Required by Financial Instruments and Exchange Act to provide sufficient information for investors to make investment decisions. - Toward the improvement of non-financial information disclosure in the annual securities report, "Principles for the Disclosure of Narrative Information," which provide a guidance about desirable disclosure and an approach for disclosure, was published in March 2019. - Prepared based on principle-based approach with a limited predefined indicators.
Corporate Governance Report (2019/Japan)	- Required by the stock exchange to provide information about the status of corporate governance for investors. - Specific disclosure items and indicators regarding corporate governance are defined pursuant to rule-based approach.

Source: Government Pension Investment fund (2019) "Study of ESG Information Disclosure" (Nissay Asset Management) p10-11 (edited slightly)

4-3 Further points for consideration

Platforms for disclosure

The number of companies choosing to publish integrated reports, aimed mostly at investors, for their voluntary ESG disclosure is rising every year. There are also companies which aim disclosure at a broader range of stakeholders by publishing a wide range of ESG information in a sustainability report, CSR report, environmental report or similar (some companies who disclose a lot of quantitative information also create data books, etc.). In addition to these publications, many companies also create a related page on their website to publish ESG information.

Listed companies will need to make appropriate decisions on what disclosure platform to use, and whether their information is aimed at mainly investors or other stakeholders, by considering the needs of investors and other stakeholders for ESG information, the contents of the information, and its importance, etc.

English disclosure

It is recommended that listed companies disclose and provide their ESG information in English so that overseas investors can easily access the information, taking into account what proportion of your investors are overseas.

Third-party assurance of ESG data

As ESG investment grows and deepens, the importance of ESG information for making investment decisions and for engagement is also growing. From this perspective, it is expected that demand will rise from investors for companies' ESG information to be assured by a third party, to ensure its reliability.

Inset 4.2: Disclosing ESG information via TDnet

In December 2019, Tokyo Stock Exchange updated its "TDnet" (Timely Disclosure network) system, which notifies investors of releases of company information, to allow the disclosure and use of ESG information via the system to improve its convenience for investors.

Specifically, there is now a specific option to make it easier for companies to register their ESG-related reports (any materials including ESG information, for example integrated reports, annual reports, sustainability reports, CSR reports, environmental impact reports, etc.) on the TDnet system (there are also options for English-language ESG reports).

ESG-related reports registered on TDnet are shared with investors in the following ways:

1. They are included on each company's page on the JPX website's "Listed Company Search"* function. This function allows investors to see company information such as financial results, timely disclosure on corporate actions, etc., articles of incorporation, AGM notices, and corporate governance reports. Including ESG-related reports in the same place creates a platform enabling access to all the information investors both in Japan and abroad need to choose new investee companies, evaluate corporate value and make investment decisions with a more mid- to long-term outlook.
2. They are included in the TDnet Database Service (TDnetDBS)**. This service allows subscribers to search for and view information registered on TDnet in the past five years for all companies listed on an exchange in Japan. Adding ESG-related reports enables subscribers to search for just companies who have registered ESG information. TSE-listed companies can access the same information through the Listed Company Database***.
3. Information registered on TDnet is automatically sent out to media outlets and information vendors. This enables the information to reach a wider range of stakeholders.

For a listed company, TDnet could be a very useful way to make sure that the ESG-related reports you make reach a wide range of investors and other stakeholders, so please consider using it.

*Listed Company Search:

https://www.jpx.co.jp/english/listing/co-search/index.html

**TDnetDBS:

https://www.jpx.co.jp/english/markets/paid-info-equities/reference/05.html

***Listed Company Database (Japanese only, TDnet ID and password required)

https://www.dwd4.tdnet.info/dbsl/jsp/main.jsp

4-4 Two-way engagement with investors

"Purposeful dialogue"

When aiming for mid- to long-term value creation, it is important to engage with investors based on the information you disclose. Engagement can also be called "purposeful dialogue". As written in the Stewardship Code and Corporate Governance Code, institutional investors are being asked to carry out constructive "purposeful dialogue" (engagement) based on in-depth knowledge of their investee companies and the companies' business environments. Engagement enables investors to deepen their understanding of how a company is responding to and working on issues including ESG from a risk and opportunity perspective. This knowledge is then used in investment decisions and the results reported to pension funds and other asset owners.

For companies, this kind of dialogue provides a good opportunity to give more in-depth information to investors about the company's response to ESG issues, the thinking behind that response and its connection to corporate value. However, it is also an opportunity to hear the investor's point of view, and can be a springboard for new ideas, growth and innovation which can lead to improvements in your business, so companies should actively take part.

Other types of engagement

Engagement with investors is not just for ESG issues, but covers a wide range of activities that companies carry out under the umbrella of investor relations (IR). Investors carry out engagement through activities such as the voting process, meetings with individual companies, sending out opinions to individual companies, and sometimes attending ESG briefings held by companies. In addition, recently there has been an increase in "collective engagement", where multiple investors work together to engage with a company as a group. These include the global institutional investor group Climate Action 100+, which engages constructively with companies which have a large impact on global environmental issues, encouraging them to disclose more information and decrease their greenhouse gas emissions, among other things.

Afterword

There is no definitive way of doing ESG disclosure and no format established as the norm. In addition, the goalposts are constantly moving as the ESG issues important to companies and investors change. It is possible to see responding to ESG issues and carrying out disclosure as a "journey". For these reasons, however, many companies may experience difficulties.

It is important that rather than aiming for perfection first time, companies take the first step using whatever resources or information they are able to. Having made that first move, companies can then use engagement with investors and other stakeholders to help find a suitable plan for improving corporate value over the long term within a changing environment. The next step is to move towards carrying it out. We hope that this Handbook can be a useful guide on this journey.

Appendix: Outlines of existing frameworks

This handbook refers to the following existing frameworks:

- Sustainable Stock Exchanges (SSE) Initiative: Model Guidance on Reporting ESG Information to Investors ("SSE Model Guidance")
- Ministry of Economy, Trade and Industry (METI): Guidance for Integrated Corporate Disclosure and Company-Investor Dialogues for Collaborative Value Creation - ESG integration, non-financial information disclosure and intangible assets into investment ("Guidance for Collaborative Value Creation")
- Recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) ("TCFD Recommendations")
- Sustainability Accounting Standards Board (SASB) Standards
- International Integrated Reporting Council (IIRC): International Integrated Reporting Framework ("IIRC Framework")
- Global Reporting Initiative (GRI) Standards
- World Federation of Exchanges (WFE): ESG Guidance and Metrics

■ Sustainable Stock Exchanges Initiative: Model Guidance on Reporting ESG Information to Investors

- What is the SSE Initiative?

The Sustainable Stock Exchanges (SSE) Initiative was set up as a UN Partner Program in 2009 aimed at the world's stock exchanges, and is organised by the UN Conference on Trade and Development (UNCTAD), the UN Global Compact, the UN Environment Programme Finance Initiative (UNEP FI), and the Principles for Responsible Investment (PRI). As of February 2020 there are 90 member exchanges. The Initiative is a platform for members to deliberate amongst themselves and learn about issues such as how to promote sustainable finance and what can be done to help companies with their ESG activities and to improve performance, while collaborating with investors, regulators, listed companies, and other stakeholders. JPX joined the SSE Initiative in December 2017.

- SSE Model Guidance

SSE published its "Model Guidance on Reporting ESG Information to Investors: A Voluntary Tool For Stock Exchanges to Guide Issuers" in 2015 as a guide for member exchanges. The Guidance was intended as a model for exchanges to use when writing bespoke guidance for their own listed companies on ESG disclosure, and sets out points and views it sees as useful to include in those guidelines (see next page for a list of contents).

JPX created and published a Japanese translation of the Model Guidance in June 2019.

- Access links/related information

The Model Guidance on Reporting ESG Information to Investors: A Voluntary Tool For Stock Exchanges to Guide Issuers can be downloaded from the SSE website:
https://sseinitiative.org/publication/model-guidance-on-reporting-esg-information-to-investors-a-voluntary-tool-for-stock-exchanges-to-guide-issuers/

The Japanese translation of the Model Guidance can be accessed from the JPX website:
https://www.jpx.co.jp/corporate/news/news-releases/0060/nlsgeu000004239v-att/SSE_Initiatives_j.pdf

SSE Initiative website:
https://sseinitiative.org/

SSE Model Guidance: Front page and contents

Original

JPX Japanese translation

1. Overview
1.1 What is ESG?
1.2 Why report on ESG considerations?
1.2.1 Investor interest in ESG factors
1.2.2 Getting ahead of regulatory developments
1.2.3 Strengthening financial performance
2. Guiding principles of report preparation
2.1 Responsibility and oversight
2.2 Clarity of purpose
2.2.1 Supporting corporate strategy
2.2.2 Identifying and understanding the audience
2.3 Relevance and materiality
2.3.1 Identifying themes
2.3.2 Adopting relevant performance indicators
2.4 Accessibility
2.5 Credibility and responsiveness
2.5.1 Robust internal ESG data collection and management processes
2.5.2 Engaging for continuous improvement
2.5.3 Assessment and assurance

Source: SSE Initiative (2015) "Model Guidance on Reporting ESG Information to Investors: A Voluntary Tool For Stock Exchanges to Guide Issuers"; JPX (2019) "ESG jōhō no hōkoku ni kansuru kigyō muke moderu gaidansu"

■ Ministry of Economy, Trade and Industry: Guidance for Collaborative Value Creation

The Japanese Ministry of Economy, Trade and Industry (METI) released their "Guidance for Integrated Corporate Disclosure and Company-Investor Dialogues for Collaborative Value Creation - ESG integration, non-financial information disclosure and intangible assets into investment" in 2017. The Guidance was based on a proposal by the Study Group on Long-term Investment (Investment evaluating ESG Factors and Intangible Assets) toward Sustainable Growth, which was set up by METI. It formulated and proposed a basic framework for promoting dialogue between companies and investors and for enhancing the quality of information disclosure, in the hope that it would serve as guidance for voluntary and proactive initiatives.

- Important features of the Guidance

The Guidance is intended to deepen mutual understanding between companies and investors through information disclosure and dialogue/engagement and promote collaborative activities to create sustainable value. From that viewpoint, the Guidance is expected to fulfill two main roles:

1. As a guideline for corporate managers and directors

First, the Guidance is expected to serve as a guideline according to which corporate managers and directors are able to comprehensively communicate key information to investors, including their management philosophies, business models, strategies and governance systems. As a direct goal, the Guidance aims to promote corporate information disclosure and enhance the quality of company-investor dialogue. Through efforts to achieve this goal, corporate managers and directors are expected to review their approaches to business management and take further actions with a view to creating corporate value.

2. As a guideline for investors

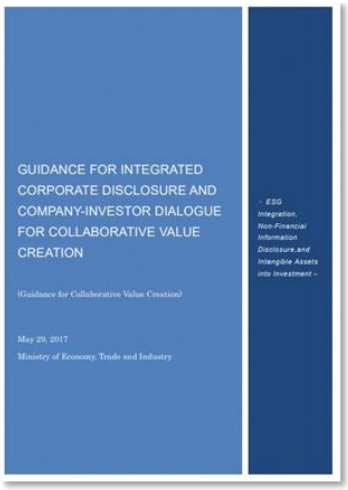
Second, the Guidance is expected to serve as a guideline for investors in evaluating companies from a long-term perspective, making investment decisions, and conducting stewardship activities. Instead of waiting for companies to provide the information with respect to the items in the Guidance, investors and analysts are expected to initiate dialogue with companies in order to obtain the information necessary for their investment decisions and remedy any information/perception gaps by referring to the Guidance. The Guidance is also designed to be used as a framework for investors to monitor investee companies and conduct dialogue to fulfill their stewardship responsibilities. It is expected that the Guidance will not only be used when institutional investors engage in stewardship activities themselves, but also when asset owners hold dialogue with asset managers.

- Access links/related information

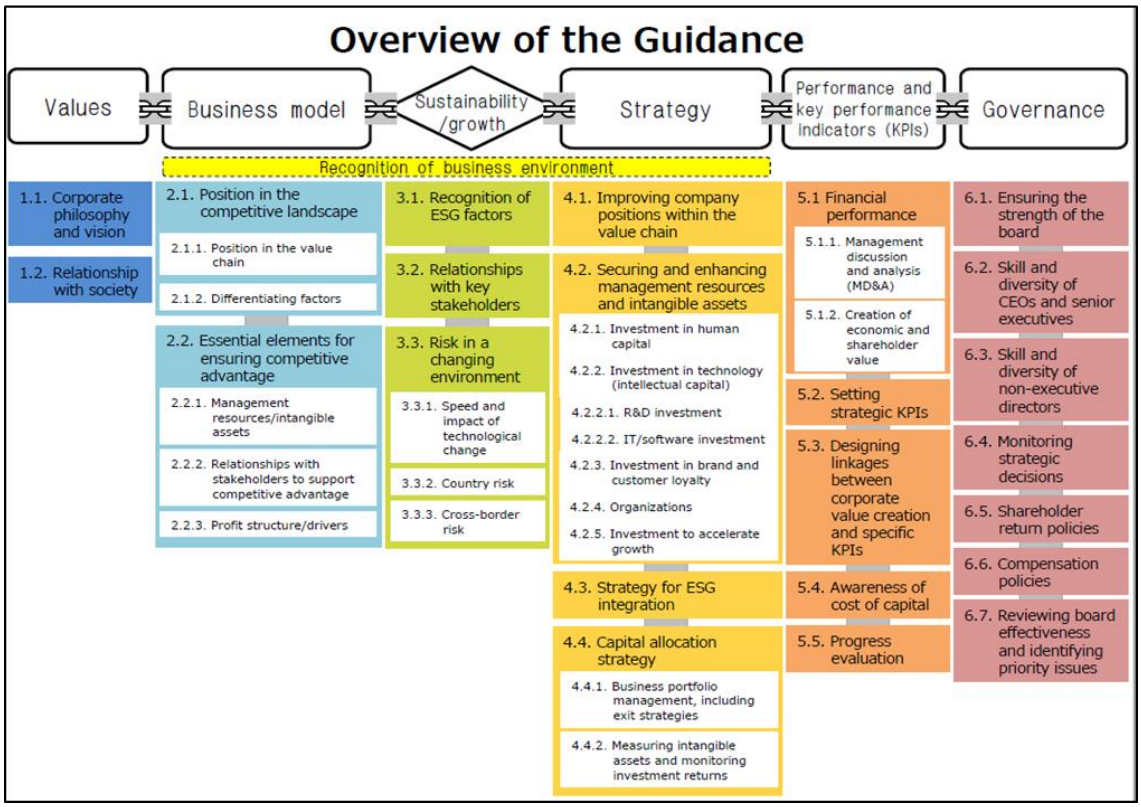
METI's Guidance for Collaborative Value Creation can be downloaded from the METI website: https://www.meti.go.jp/english/press/2017/pdf/0529_004b.pdf

METI's Guidance for Collaborative Value Creation: front page and overview

Original



English translation



Source: METI (2017) "Kachi kyōsō no tame no sōgōteki kaiji/taiwa gaidansu – ESG/hizaimujōhō to mukei shisan tōshi"; METI (2017 translation) "Guidance for Integrated Corporate Disclosure and Company-Investor Dialogues for Collaborative Value Creation - ESG integration, non-financial information disclosure and intangible assets into investment"

■ Recommendations of the Task Force on Climate-related Financial Disclosures (TCFD)

- What is TCFD?

The Task Force on Climate-Related Financial Disclosures (TCFD) was set up in December 2015 by the Financial Stability Board (FSB), at the request of the G20 Finance Ministers and Central Bank Governors meeting, to consider disclosure of climate-related information and how financial institutions should react to climate change. The Task Force deliberated with the aim of creating recommendations to encourage information disclosure with the consistency, comparability, credibility, and clarity needed for appropriate investment decisions based on climate change metrics. They published their Final Recommendations in June 2017. The number of companies and organisations worldwide which have officially expressed support for the Recommendations is growing, and stands at over 1050 as of February 2020. Of any single country, Japan has the most TCFD supporters with other 240. JPX expressed its support in October 2018.

- The composition of the Recommendations

The Recommendations published in June 2017 are made up of three publications:

Final Report: Recommendations of the Task Force on Climate-Related Financial Disclosures

This is the main report which is often referred to as the "TCFD Recommendations". After an explanation on climate-related risks, opportunities and financial impacts, it sets out "Recommendations and Guidance" which apply to all sectors, financial and non-financial. In addition, it writes about the need for scenario analysis and recommends how to approach it.

Original

Japanese translation

Annex: Implementing the Recommendations of the TCFD

This is supplemental guidance for a) the financial sector and b) non-financial sectors, which are expected to be more heavily impacted by climate change and the shift to a low-carbon economy. It provides more detailed guidance for each sector: banks, insurance companies, asset owners, and asset managers for the financial sector, and energy, transportation, materials and buildings, and agriculture, food, and forest products for non-financial sectors, taking into account their differences.

Technical Supplement: The Use of Scenario Analysis in Disclosure of Climate-Related Risks and Opportunities

This technical supplemental report sets out the details of "scenario analysis" and key things to think about when applying it, in order to support companies in creating disclosure based on the TCFD Recommendations.

TCFD recommends that companies be aware of the "risks" and "opportunities" arising from climate change that could affect their business activities, and disclose on the following four topics:

- Governance: What kind of governance structure is in place to consider climate change and is this reflected in company management?
- Strategy: What kind of impact will climate change have on company management in the short, medium, and long term? How did you come to these conclusions?
- Risk Management: How do you identify and evaluate climate-related risks, and how are you trying to mitigate these?
- Metrics and Targets: What metrics do you use to identify risks and opportunities and measure progress towards targets?

- TCFD in Japan

In May 2019, a Japanese "TCFD Consortium" was launched as a platform for debate on how to make company disclosure based on the TCFD Recommendations more effective, and how to make sure that it leads to more appropriate investment decisions from financial institutions. The Consortium is comprised of a General Meeting, Planning Committee, Working Group for information disclosure, Working Group for information usage, and outreach events.

As a result of deliberations by the Working Group for information usage on how investors can use TCFD-based disclosure, in October 2019 the Consortium published its Guidance for Utilizing Climate-related Information to Promote Green Investment ("Green Investment Guidance", https://tcfd-consortium.jp/en/news_detail/19100802). The Guidance provides commentary on perspectives investors need to consider to understand TCFD-based disclosures, and for companies, provides a way

to better understand the perspectives of investors and other stakeholders.

The Working Group for information disclosure on the other hand, which debates topics such as specific contents of TCFD-based disclosure, has been working on an update of the Ministry of Economy, Trade and Industry's Guidance for Climate-related Financial Disclosures ("TCFD Guidance", https://www.meti.go.jp/english/press/2018/1225_006.html), which was first published in August 2018. This TCFD Guidance was written by METI's "TCFD Study Group on Implementing TCFD Recommendations for mobilizing green finance through proactive corporate disclosures" and aims to provide information and case examples to explain approaches to TCFD-based disclosure, as well as industry-based viewpoints that companies should take to show their efforts.

Outside of the TCFD Consortium, the Japanese Ministry of the Environment (MOEJ) has also been active, running a support program for companies to analyse their own climate risks and opportunities in line with the TCFD Recommendations from FY2018. This led to the creation of a Practical Guide for Scenario Analysis in Line with TCFD Recommendations, published in March 2019 (https://www.env.go.jp/en/headline/2396.html), which brought together examples from the companies within the program. MOEJ released a 2nd Edition (https://www.env.go.jp/en/headline/2439.html) in March 2020, adding a) scenario analysis key points of practice, b) practical examples from 12 companies supported by MOEJ in 2019, and c) useful materials for scenario analysis.

- Access links/related information

The TCFD Recommendations can be downloaded from the TCFD website.
https://www.fsb-tcfd.org/publications/

A Japanese translation of the Final Recommendations can also be downloaded from the TCFD website.
https://www.fsb-tcfd.org/wp-content/uploads/2017/06/TCFD_Final_Report_Japanese.pdf

Related information, including the Green Investment Guidance, can be found on the TCFD Consortium website.
https://tcfd-consortium.jp/en

Sustainability Accounting Standards Board (SASB) Standards

- What is SASB?

The Sustainability Accounting Standards Board (SASB) is a non-profit organisation which was set up in San Francisco, USA in 2011. Looking to improve the quality of company reporting so it can contribute to the decision-making process of mid- to long-term focused investors, SASB has set disclosure standards relating to ESG issues that it identifies as reasonably likely to have material impacts on companies in the future.

- The SASB Standards

After its launch, SASB spent around six years conducting debate and analysis together with experts, investors, academics and others, and in November 2018, published disclosure standards for 77 industries within 11 sectors.

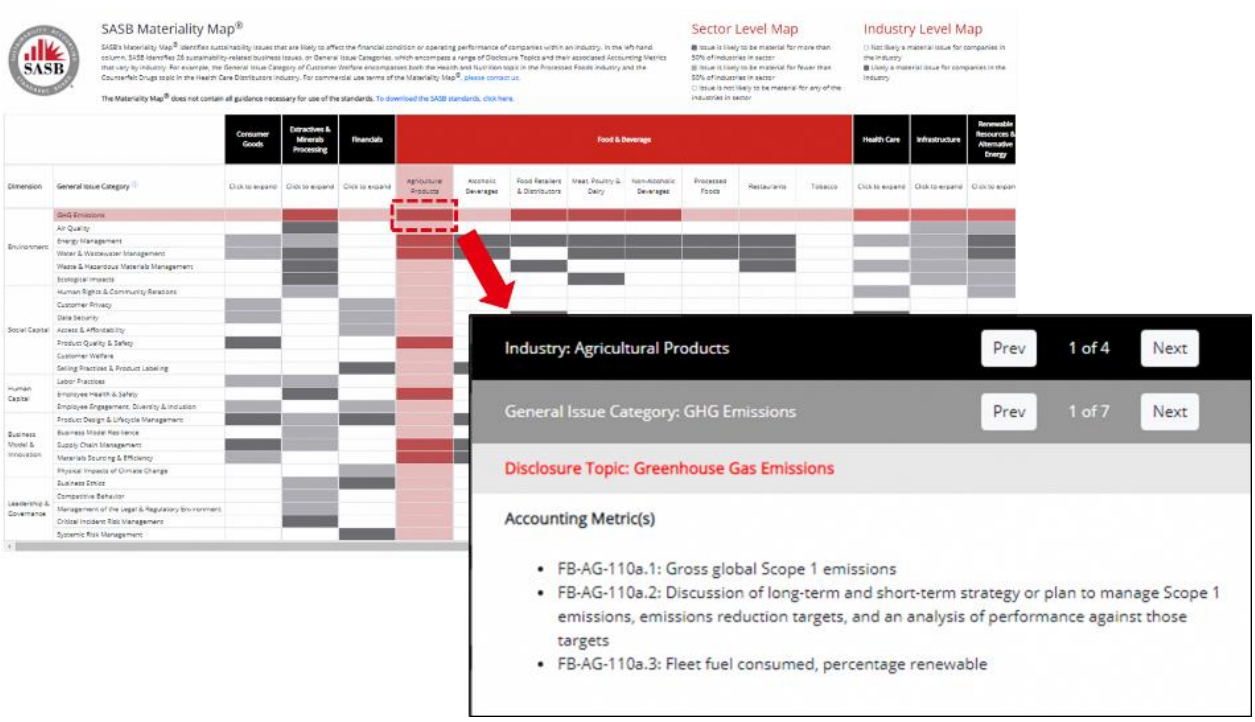
Intended to help analyse a company's sustainability, the SASB Standards are based on 26 "General Issue Categories" organised under five "Dimensions", as shown below.

Dimension	**Environment**	**Social Capital**	**Human Capital**	**Business Model & Innovation**	**Leadership & Governance**
General Issue Category	GHG emissions Air quality Energy management Water & wastewater management Waste & hazardous materials management Ecological impacts	Human rights & community relations Customer privacy Data security Access & affordability Product quality & safety Customer welfare Selling practices & product labeling	Labour practices Employee health & safety Employee engagement, diversity & inclusion	Product design & lifecycle management Business model resilience Supply chain management Materials sourcing & efficiency Physical impacts of climate change	Business ethics Competitive behaviour Management of the legal & regulatory environment Critical incident risk management Systemic risk management

Source: SASB website

Disclosure Topics and Accounting Metrics are then set for each of the General Issues judged to be material for each particular industry, and set out in detail in the Standards. Disclosure Topics and Accounting Metrics for each sector/industry can also be found in the SASB Materiality Map (https://materiality.sasb.org/). The image on the next page shows Disclosure Topics and Accounting Metrics for the agricultural products industry as shown on the Materiality Map.

The SASB Materiality Map



Source: SASB Materiality Map

- Other tools from SASB

As well as the Standards, SASB have also published reports on topics such as disclosure of sustainability information and engagement. For example, the Engagement Guide for Asset Owners and Asset Managers (https://www.sasb.org/knowledge-hub/engagement-guide/) gives investors guidance on how to engage with investee companies. SASB plans to translate this Guide into Japanese.

To aim for implementation of TCFD-based disclosure, SASB has also published a TCFD Implementation Guide (https://www.sasb.org/knowledge-hub/tcfd-implementation-guide/) in co-operation with the Climate Disclosure Standards Board (CDSB), and has translated this into Japanese (https://www.sasb.org/knowledge-hub/tcfd-implementation-guide-japanese/).

- Access links/related information

The SASB Standards are currently only available in English, but can be downloaded from the SASB website:
https://www.sasb.org/standards-overview/download-current-standards/

International Integrated Reporting Council (IIRC): International Integrated Reporting Framework ("IIRC Framework")

- What is IIRC?

The International Integrated Reporting Council (IIRC) is a global coalition of regulators, investors, companies, standard setters, the accounting profession, academia and NGOs which was set up in the UK in 2010 by A4S (The Prince's Accounting for Sustainability Project) and GRI (Global Reporting Initiative). Among its aims are to improve the quality of information available to providers of financial capital and promote a more cohesive and efficient approach to corporate reporting.

- The IIRC Framework and its objectives

IIRC published The International <IR> Framework[25], setting out its position on the crafting of integrated reports, in 2013, and since then, integrated reporting in Japan and around the world has progressed massively. In February 2020, IIRC announced that a revision of the Framework is underway.

The Framework, as explained in the executive summary, "promotes a more cohesive and efficient approach to corporate reporting and aims to improve the quality of information available to providers of financial capital to enable a more efficient and productive allocation of capital… The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value over time. An integrated report benefits all stakeholders interested in an organization's ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers."

- Main elements of the IIRC Framework

1. Integrated Thinking

The IIRC Framework hopes that rather than companies just collecting various bits of information and reporting them in one place, the report preparation process will cause "integrated thinking" (the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects) to spread through each company, leading to changes in their actions and improved corporate value.

2. Guiding Principles

The IIRC Framework sets Guiding Principles to underpin the preparation of an integrated report: Strategic focus and future orientation; Connectivity of information; Stakeholder relationships; Materiality; Conciseness; Reliability and completeness; Consistency and comparability.

[25] IIRC "The <IR> Framework Revision: Inspiring better reporting" <https://integratedreporting.org/news/the-ir-framework-revision-inspiring-better-reporting/>

3. Content Elements

The Framework defines eight "Content Elements" which must be included in an integrated report. These are fundamentally linked to each other and are not mutually exclusive.

- Organizational overview and external environment: What does the organisation do and what are the circumstances under which it operates?
- Governance: How does the organisation's governance structure support its ability to create value in the short, medium and long term?
- Business model: What is the organisation's business model?
- Risks and opportunities: What are the specific risks and opportunities that affect the organisation's ability to create value over the short, medium and long term, and how is the organisation dealing with them?
- Strategy and resource allocation: Where does the organisation want to go and how does it intend to get there?
- Performance: To what extent has the organisation achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals?
- Outlook: What challenges and uncertainties is the organisation likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?
- Basis of presentation: How does the organisation determine what matters to include in the integrated report and how are such matters quantified or evaluated?

The chart on the next page shows how these link to each other and to the value creation process.

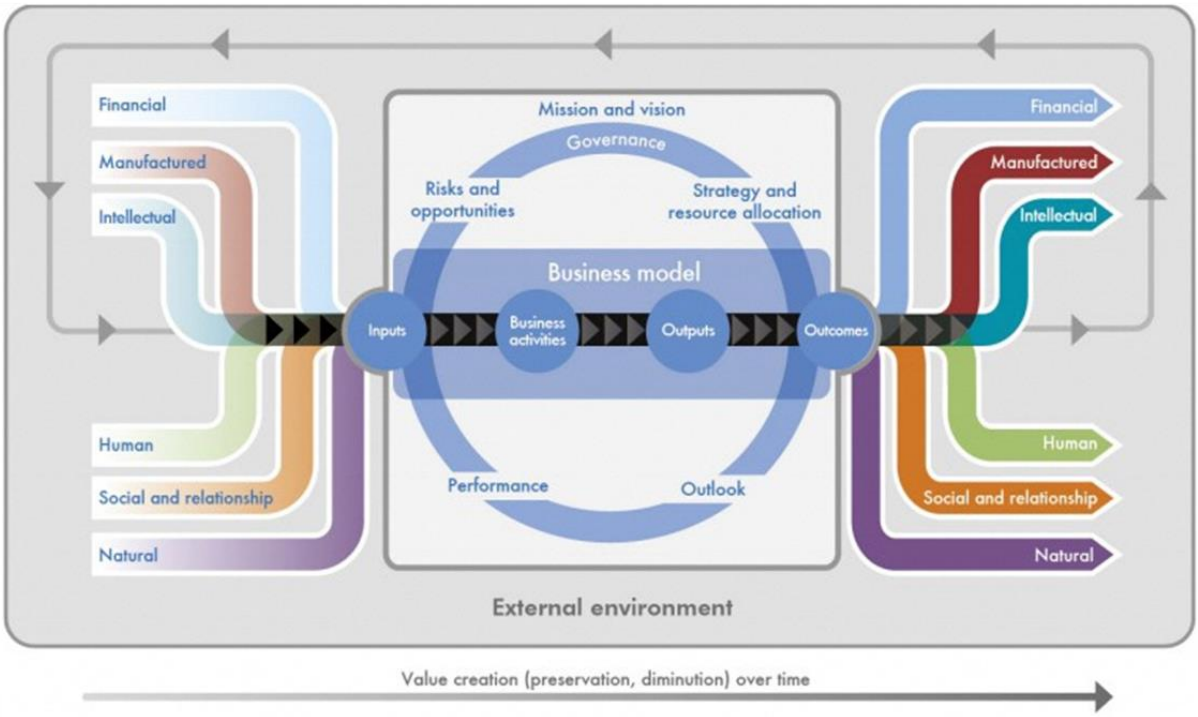
- Access links/related information

The English and Japanese versions of the IIRC Framework can be downloaded from the IIRC website.
https://integratedreporting.org/resource/international-ir-framework/

IIRC Framework: front pages and chart of the value creation process

Original

Japanese translation



Source: IIRC (2013) "International <IR> Framework"

Global Reporting Initiative (GRI) Standards

- What is GRI?

The Global Reporting Initiative (GRI) was founded in 1997 by US non-profit the Coalition for Environmentally Responsible Economies (CERES) and the UN Environment Program (UNEP), among others, to encourage understanding and support the creation of sustainability reports among organisations such as private companies and government agencies. It is currently based in Amsterdam, the Netherlands.

- The GRI Standards

GRI released its first "GRI Guidelines" in 2000. After discussions with various stakeholders including companies, NGOs, consultants, auditors, institutional investors, labour unions, and academics, it released the fourth generation (G4) in 2013. Then, as the situation with sustainability reports progressed, in 2016 it released the GRI Standards, an enhanced version of the Guidelines.

The GRI Standards see importance in not only what ESG issues can affect an organisation, but also how an organisation can affect society or the environment: its introduction states that "Sustainability reporting, as promoted by the GRI Standards, is an organization's practice of reporting publicly on its economic, environmental, and/or social impacts, and hence its contributions – positive or negative – towards the goal of sustainable development."

- Structure of the GRI Standards

As listed below, the GRI Standards are made up of "Universal Standards" (101, 102, and 103) and "Topic-specific Standards" (200 series, 300 series, and 400 series). The three Universal Standards are applied to all organisations preparing sustainability reports. Organisations looking to report on material issues specific to them (economic, environmental, social) can pick the relevant one from the Topic-specific Standards.

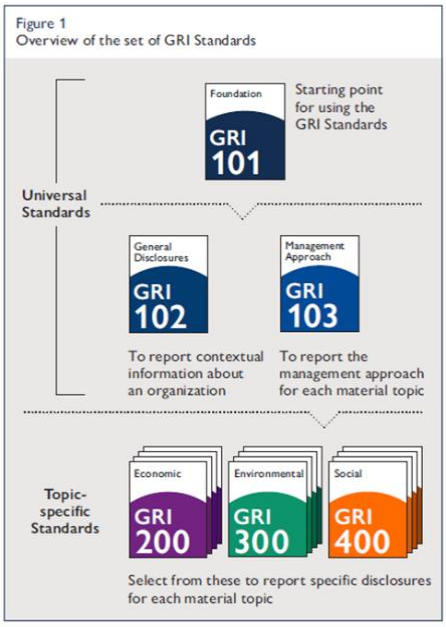
-GRI 101: Foundation - a guide to how to use the GRI Standards

-GRI 102: General Disclosures - reporting an organisation's relevant contextual information

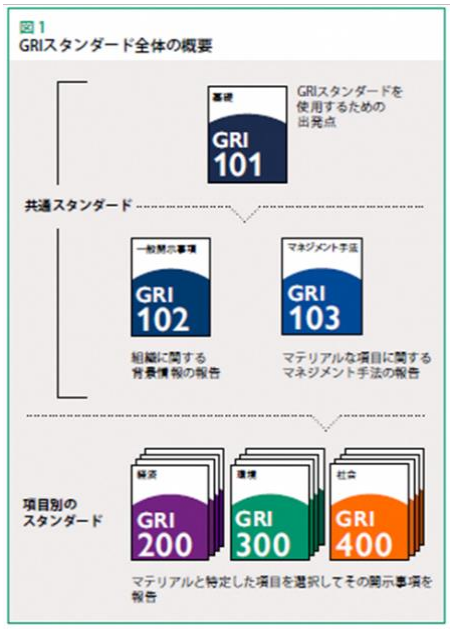
-GRI 103: Management Approach - reporting how material topics are managed

-GRI 200, 300, 400 series – data points for reporting information on an organisation's economic, environmental, and social impact.

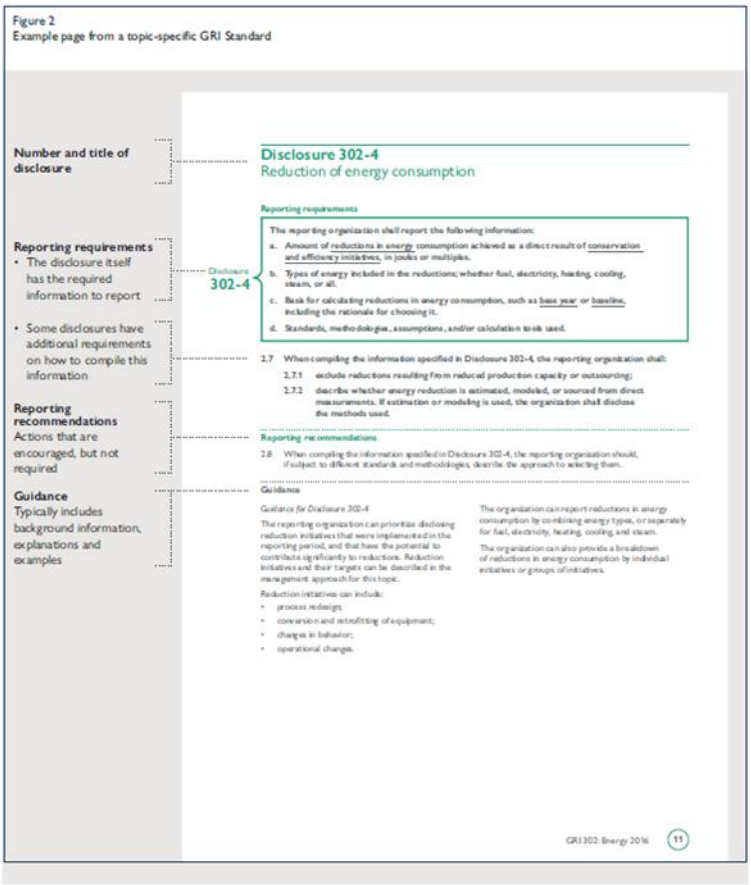
Overview of the GRI Standards and an example page from a Topic-specific Standard



Original



Japanese translation



Source: GRI (2016) "GRI Standards"

- Access links/related information

The GRI Standards can be downloaded from the GRI website.

English: https://www.globalreporting.org/standards

Japanese: https://www.globalreporting.org/standards/gri-standards-translations/gri-standards-japanese-translations-download-center/

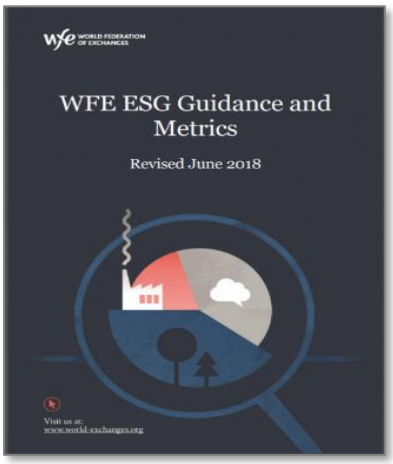
■ World Federation of Exchanges (WFE): ESG Guidance and Metrics

- What is WFE?

The World Federation of Exchanges is a global industry association for the world's main exchanges which was created in 1961, and currently has around 250 members, mostly exchanges and clearing houses. JPX is a member of WFE and its CEO has been a WFE Board member since 2019.

In 2014, WFE set up a Sustainability Working Group to help advance activity on sustainable finance and promoting ESG investment. Since then the Group has been working on things such as researching and analysing member exchanges' sustainability activities and work on promoting ESG investment, as well as creating sustainability principles and other guidance for the exchange industry. JPX has been participating in the Sustainability Working Group, and become Vice-Chair in 2018.

- WFE ESG Guidance and Metrics



WFE published its ESG Guidance and Metrics in 2015, with the aim of supplementing the SSE Model Guidance by providing a reference point for exchanges looking to encourage ESG reporting from their own listed companies. The Guidance is based around 33 disclosure metrics. In 2018, taking into account the previous year's TCFD Recommendations and other developments, WFE released an updated version of the guidance and metrics.

The Guidance gives the following four points as important for companies to consider when reporting ESG information to investors.

- Governance/responsibility and oversight: A board statement setting out how the organisation determines material issues, how these are embedded in the organisation’s strategy, how the board reviews progress against targets, etc.
- Clarity of purpose/clear link to business value: Organisations should make clear how their selected ESG issues link to value creation/destruction.
- Materiality: Organisations should explain to investors how they identify their material issues.
- Quality and frequency of reporting: Organisations should make sure that their reporting is accurate, timely, and follows one of the internationally recognised reporting standards.

Metrics introduced in the WFE ESG Guidance and Metrics

Environmental metrics	Calculation
GHG Emissions	Total amount, in CO2 equivalents, for a) Scope 1, b) Scope 2, c) Scope 3
Emissions Intensity	Total a) GHG and b) non-GHG emissions per output scaling factor chosen by company (revenues, sales, production units, etc.)
Energy Usage	Total amount of energy a) directly and b) indirectly consumed
Energy Intensity	Total direct energy usage per output scaling factor chosen by company (physical space, full time employees, revenues, etc.)
Energy Mix	Percentage: energy usage by generation type (renewables, gas, etc.)
Water Usage	Total amount of water a) consumed and b) reclaimed
Environmental Operations	a) Does your company follow a formal Environmental Policy? Yes/No; b) Does your company follow a specific waste, water, energy, and/or recycling policy? Yes/No; c) Does your company use a recognized energy management system (ISO 50001, etc.) Yes/No
Environmental Oversight (1)	Does your Board/Management Team oversee and/or manage climate-related risks? Yes/No
Environmental Oversight (2)	Does your Board/Management Team oversee and/or manage other sustainability issues? Yes/No
Climate Risk Mitigation	Total amount invested, annually, in climate-related infrastructure, resilience, and product development
Social metrics	**Calculation**
CEO Pay Ratio	Ratio: CEO total compensation to median FTE total compensation
Gender Pay Ratio	Ratio: Median male compensation to median female compensation
Employee Turnover	Percentage: year-over-year change for a) full-time employees, b) part-time employees, c) contracts and/or consultants
Gender Diversity	Percentage: a) total enterprise headcount, b) entry- and mid-level positions, c) senior- and executive-level positions held by women
Temporary Worker Ratio	Total enterprise headcount held by a) part-time employees, b) contractors and/or consultants
Non-Discrimination	Does your company follow a sexual harassment and/or non-discrimination policy? Yes/No
Injury Rate	Percentage: Frequency of injury events relative to total workforce time
Global Health & Safety	Does your company follow an occupational health and/or global health & safety policy? Yes/No
Child & Forced Labor	a) Does your company follow a child and/or forced labor policy? Yes/No; b) If yes, does your child and/or forced labor policy also cover suppliers and vendors? Yes/No
Human Rights	a) Does your company follow a human rights policy? Yes/No; b) If yes, does your human rights policy also cover suppliers and vendors? Yes/No
Governance metrics	**Calculation**
Board Diversity	Total a) board seats and b) committee chairs occupied by men and women
Board Independence	a) Does company prohibit CEO from serving as board chair? Yes/No; b) Percentage: Total board seats occupied by independents
Incentivized Pay	Are executives formally incentivized to perform on sustainability? Yes/No
Collective Bargaining	Percentage: Total enterprise headcount covered by collective bargaining agreement(s)
Supplier Code of Conduct	a) Are your vendors or suppliers required to follow a Code of Conduct? Yes/ No; b) If yes, what percentage of your suppliers have formally certified their compliance with the code?
Ethics & Anti-Corruption	a) Does your company follow an Ethics and/or Anti-Corruption policy? Yes/No; b) If yes, what percentage of your workforce has formally certified its compliance with the policy?
Data Privacy	a) Does your company follow a Data Privacy policy? Yes/No; b) Has your company taken steps to comply with GDPR rules? Yes/No
Sustainability Reporting	Does your company publish a sustainability report? Yes/No
Disclosure Practices	a) Does your company provide sustainability data to sustainability reporting frameworks? Yes/No; b) Does your company focus on specific UN SDGs? Yes/No; c) Does your company set targets and report progress on the UN SDGs? Yes/No
External Assurance	Are your sustainability disclosures assured or validated by a third party? Yes/No

Source: WFE (2018) "WFE ESG Guidance and Metrics" (slightly edited)

- Access links/related information

The WFE ESG Guidance and Metrics can be downloaded from the WFE website.

https://www.world-exchanges.org/news/articles/world-federation-exchanges-publishes-revised-esg-guidance-metrics

Practical Handbook for ESG Disclosure

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JPX