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1 Setting the Scene – Sources and Overview

1.1 What are the main substantive ESG-related regulations and who is driving the regulatory agenda in your jurisdiction?

In Japan, there is no law that comprehensively covers ESG issues, but various laws regulate ESG-related matters.

First, with regard to the environment, based on the *Basic Act on the Environment* (Act No. 91 of 1993), various domestic laws concerning environmental measures have been enacted, such as the *Act on Promotion of Global Warming Countermeasures* (Act No. 117 of 1998), the *Climate Change Adaptation Act* (Act No. 50 of 2018), the *Basic Act on Biodiversity* (Act No. 58 of 2008), the *Act on Prevention of Marine Pollution and Maritime Disaster* (Act No. 136 of 1970), the *Soil Contamination Countermeasures Act* (Act No. 53 of 2002), the *Water Pollution Prevention Act* (Act No. 138 of 1970), and the *Air Pollution Control Act* (Act No. 97 of 1968), etc. The Ministry of the Environment, as the competent authority, addresses these numerous environmental issues.

With regard to society at large, various labour laws address the issue of discriminatory treatment and harassment in the workplace. For example, the *Labor Standards Act* (Act No. 49 of 1947) prohibits unreasonable discrimination on the grounds of nationality, social status, gender, and other factors. The *Act on Equal Opportunity and Treatment between Men and Women in Employment* (Act No. 113 of 1972) prohibits unreasonable discrimination on the basis of gender in hiring, promotion, transfer, etc., and imposes on employers the obligation to establish a system necessary to deal with sexual harassment issues. In addition, the *Act on the Promotion of Women's Active Engagement in Professional Life* (Act No. 64 of 2015) stipulates various measures to promote the advancement of women, such as the obligation to disclose differences in wages between men and women to companies of a certain size or larger. Furthermore, the *Act on Comprehensively Advancing Labor Measures, and Stabilizing the Employment of Workers, and Enriching Workers' Vocational Lives* (Act No. 132 of 1966) obliges employers to take measures to prevent power harassment and SOGI (sexual orientation and gender identity) harassment. In addition, regulations have been established to promote or stabilise the employment of the disabled and the elderly, such as the *Act to Facilitate the Employment of Persons with Disabilities* (Act No. 123 of 1960) and the *Act on Stabilization of Employment of Elderly Persons* (Act No. 68 of 1971). The Ministry of Health, Labour and Welfare (MHLW) is the competent authority for all of these laws.

With regard to governance, the Japan's Corporate Governance Code (CG Code), the securities listing regulations of the Tokyo Stock Exchange, plays an important role. The CG Code provides concrete guidelines not only on corporate governance, but also for corporate initiatives for sustainability.

1.2 What are the main ESG disclosure regulations and how have they evolved during the past 12 months?

The statutory disclosure under the *Financial Instruments and Exchange Act* (Act No. 25 of 1948) is one of the main ESG-relevant disclosure regulations. In January 2023, an amendment to the *Cabinet Office Order on Disclosure of Corporate Affairs* (Ministry of Finance Order No. 5 of 1973) made it mandatory to disclose sustainability information in annual securities report, a continuous disclosure document for listed companies, in and after the fiscal year ending March 2023. Specifically, a new section titled "Approach and Initiatives Relating to Sustainability" was added to the "Business Overview" section of the annual securities report, requiring companies to report on four items: governance; strategy; risk management; and metrics and targets. Of these, all companies are required to include "Governance" and "Risk Management". For "Strategy" and "Metrics and Targets", all companies are required to include matters related to human capital, while other items are left to the judgment of each company based on the materiality of the information. In addition, in the "Employees" section, companies are required to disclose diversity indicators, such as the ratio of female managers, the percentage of male employees taking childcare leave, and the wage gap between men and women.

1.3 What voluntary ESG disclosures, beyond those required by law or regulation, are customary?

In addition to the statutory disclosures described in question 1.2, above, there are voluntary ESG-relevant disclosures made by companies. Voluntary disclosures take the form of so-called CSR reports, environmental reports, integrated reports, etc., which are intended to provide information not only to shareholders and investors but also to other various stakeholders. Since there are no regulations that directly require such disclosures, it is up to individual companies to decide how they voluntarily disclose ESG-related information to their stakeholders.

In the area of climate change, since the Task Force on Climate-Related Financial Disclosures (TCFD) established under the Financial Stability Board (FSB) published its climate-related disclosure recommendations in 2017, the number of disclosures based on its recommendations has increased. As of October 2023, 1,470 companies and organisations support the recommendations of the TCFD in Japan (https://www.meti.go.jp/policy/energy_environment/global_warming/tcfd_supporters.html). For many years, Japan has been recognised as one of the countries with the largest number of supporting companies and organisations in the world.

1.4 Are there significant laws or regulations currently in the proposal process?

Currently, there are no particular laws or regulations that directly addresses ESG issues, nor are there any in the proposal process. However, a new set of laws or regulations to mandate ESG disclosures in Japan is currently being discussed by a panel of experts within the government. On 29 March 2024, the Sustainability Standards Board of Japan (SSBJ) published an exposure draft, and the Financial System Council's Working Group on Sustainability Information Disclosure and Assurance is now discussing it. There are three public drafts from the SSBJ: (i) the Universal Sustainability Disclosure Standard Exposure Draft "Application of the Sustainability Disclosure Standards"; (ii) Theme-based Sustainability Disclosure Standards Draft No.1 "General Disclosures"; and (iii) Theme-based Sustainability Disclosure Standard Exposure Draft No.2 "Climate-related Disclosures".

The development of the new laws and regulations is expected to lead to mandatory ESG disclosure in Japanese annual securities reports in the future, and as early as the fiscal year ending 31 March 2027, all Japanese-listed companies (including foreign companies) on the Tokyo Stock Exchange may be required to disclose information based on the TCFD's recommendations (Governance, Strategy, Risk Management, and Metrics and Targets) in their annual securities reports.

1.5 What significant private sector initiatives relating to ESG are there? To what extent are private companies reporting on ESG issues?

A number of companies are taking a variety of approaches to ESG issues. These are not being addressed uniformly, but they include setting targets for reducing CO_2 emissions, expanding the use of renewable energy, protecting water resources, using recycled materials, among other things.

In addition, by 3 March 2024, 1,013 Japanese companies had obtained or committed to obtain certification for Science Based Targets (SBT), a climate target certification that is reviewed and certified by the Science Based Targets Initiative (SBTi) (https://sciencebasedtargets.org), a global initiative. This number nearly doubled from May 2023.

As of October 2024, 88 Japanese companies are participating in RE100, a collaborative initiative that commits to 100% renewable energy for electricity used by influential companies around the world in their business operations (https://japan-clp.jp/en).

2 Principal Sources of ESG Pressure

2.1 What are the views and perspectives of investors and asset managers toward ESG, and how do they exert influence in support (or in opposition) of those views?

Many investors and asset managers recognise that ESG awareness is essential for companies to gain market share and profits. According to "Global Sustainable Investments 2022" (https://www.gsi-alliance.org/wp-content/uploads/2023/12/GSIA-Report-2022.pdf), the proportion of ESG investments in Japan relative to total managed assets has increased from 24% to 34% from 2020 to 2022 (about 30% increase from 3% in 2016). Japan's ESG investments increased from US$474 billion in 2016, and US$2,784 billion in 2020, to US$4,289 billion in 2022 (page 11 of the aforementioned report).

2.2 What are the views of other stakeholders toward ESG, and how do they exert influence in support (or in opposition) of those views?

Other stakeholders are also increasingly concerned about ESG issues, particularly in their demand for the proactive disclosure of information on climate change and sustainability. With respect to climate change, as discussed in question 2.5 below, there have been cases where litigious action has been taken.

2.3 What are the principal regulators with respect to ESG issues, and what issues are being pressed by those regulators?

In Japan, there is no competent authority directly responsible for ESG issues, and various authorities regulate these issues.

In addition to taking steps to enhance corporate ESG disclosure, the Financial Services Agency (FSA) is enhancing the credibility and transparency of ESG investments by promoting sustainable finance, formulating a Code of Conduct for ESG Evaluation and Data Providers (https://www.fsa.go.jp/news/r4/singi/20221215/02.pdf), and establishing new guidelines for the supervision of ESG investment trusts (https://www.fsa.go.jp/news/r4/shouken/20230331-2/03.pdf).

The Ministry of the Environment has published Environmental Reporting Guidelines (https://www.env.go.jp/content/900497076.pdf) to support voluntary ESG disclosure by companies. The ministry also supports companies' green transformation to achieve the 2050 carbon-neutrality goals, and supports the introduction of renewable energy and the spread of energy-saving technologies.

The Ministry of Economy, Trade and Industry (METI) has established a study group to promote disclosure based on the TCFD recommendations and is developing guidelines, in addition to working on ESG investment issues.

Although not a government agency, the Tokyo Stock Exchange has had a considerable impact on corporate governance through the development of CG codes.

2.4 Have there been material enforcement actions with respect to ESG issues?

In Japan, there is no competent authority that regulates advertising activities in general, but the Consumer Affairs Agency (CAA), which has jurisdiction over the *Act against Unjustifiable Premiums and Misleading Representations* (Act No. 134 of 1962), regulates consumer labelling by businesses, such as advertisements claiming unfounded sustainability ("greenwashing"). In December 2022, the CAA issued an administrative order to a manufacturer and seller of plastic products that had been sold with descriptions or taglines such as "biodegradable" or "biodegradable plastic" on the packaging, stating that such labelling constituted "misleading superiority" under the said Act.

In March 2023, the FSA partially revised its Comprehensive Guidelines for the Supervision of Financial Instruments Business Operators, etc. to address global concerns (greenwashing, etc.) that investment funds with ESG in their name or investment strategy may not match their actual operating performance. Although the Guidelines are not laws, if they are violated, there is a possibility of being subject to administrative penalties, and in effect, investment funds are required to manage in accordance with the Guidelines.

2.5 What are the principal ESG-related litigation risks, and has there been material litigation with respect to ESG issues, other than enforcement actions?

If a company fails to take sufficient measures to address climate change (such as insufficient greenhouse gas emission-reduction targets), investors, environmental NGOs and consumers may file litigation seeking: (i) damages or other compensation for misrepresentations by the company regarding climate change; or (ii) direct liability for greenhouse gas emissions.

There is not a great deal of climate change-related litigation in Japan, but there are a few recent cases: in 2017, local residents filed a petition with the Sendai District Court seeking an injunction against the operation of a coal-fired power plant, claiming that their lives, health, bodies, and ecosystems would be harmed by air pollutants such as sulfur oxides and nitrogen oxides emitted by the plant's operations, as well as by the emission of CO_2 which causes climate change. A similar litigation was filed with the Kobe District Court in 2018.

Although there are no actual litigation cases in Japan, there is a risk that companies could be sued if it is discovered that there have been human rights violations or environmental destruction at its group companies or in the supply chain, and that the due diligence was inadequate. There is also a risk that investors will file a lawsuit if a company makes false ESG-related disclosures, such as when a company reports that it is taking environmental measures that it is not actually taking.

2.6 What are current key issues of concern for the proponents of ESG?

Companies must address climate change, ensure transparency in their supply chains, and improve governance. In addition, as mentioned in question 2.4, greenwashing and bluewashing are among the current key issues in light of the growing importance of ESG activities, particularly sustainability disclosure.

Disparities also exist in the level of public awareness and understanding of human rights: according to the Public Opinion Survey on Human Rights Protection (https://survey.gov-online.go.jp/r04/r04-jinken) conducted by the Cabinet Office of the Government in 2022, understanding of basic human rights tends to be higher in urban areas than in rural areas. These disparities can be attributed to factors such as the prevalence of education, ease of access to information, characteristics of local communities, and differences in social roles.

2.7 Have ESG issues attracted shareholder activism, and from whom?

Yes. Shareholder activism in general is growing in Japan. Environmental NGOs have been especially active in making shareholder proposals on climate change measures. In recent years, there have been cases in which environmental NGOs have made shareholder proposals to major Japanese financial institutions, electric power companies and trading companies on climate change measures. Although all of these shareholder proposals were rejected, some institutional investors voted in favour of them, representing approximately 20% to 30% of the votes cast.

Institutional investors also submitted a shareholder proposal calling for major automakers to disclose information about their decarbonisation activities. Although this proposal was also rejected, foreign institutional investors and environmental NGOs supported them.

3 Integration of ESG into Strategy, Business Operations and Planning

3.1 Who has principal responsibility for addressing ESG issues? What is the role of the management body in setting and changing the strategy of the corporate entity with respect to these issues?

Since ESG matters are part of the business execution of the company, the board of directors (or in the case of a company with committees, the executive officers), which makes business execution decisions, has the principal responsibility for addressing ESG issues. In other words, directors who are members of the board of directors (or in the case of a company with committees, the executive officers) owe the duty of care of a good manager to the company under the *Companies Act*, and as a part of that duty, they are also responsible for addressing ESG issues.

According to the Corporate Governance Code (https://www.jpx.co.jp/english/news/1020/b5b4pj0000046kxj-att/b5b4pj0000046l07.pdf) issued by the Tokyo Stock Exchange, the board of directors is required to take appropriate measures regarding sustainability issues (Principle 2–3). In addition, the board of directors is required to formulate a basic policy regarding its own sustainability initiatives from the perspective of improving corporate value over the medium to long term (Supplementary Principle 4–2 (2)).

The Guidelines for Investor and Company Engagement (https://www.fsa.go.jp/en/news/2021/20210611/01.pdf), issued by the FSA, state that one of the matters that investors and companies are expected to focus on in their dialogue with one another is whether or not the growing social demand and interest in ESG and SDGs are appropriately reflected in management strategies and management plans, and whether or not a framework, such as the establishment of a committee on sustainability, has been established under the board of directors or on the management side (Guidelines 1–3).

3.2 What governance mechanisms are in place to supervise management of ESG issues? What is the role of the board and board committees *vis-à-vis* management?

Under the *Companies Act* of Japan, in the case of a company that adopts the governance system of a company with auditors and that does not adopt a system with committees, the board of directors makes important decisions on the execution of business, so the function of the board of directors and the management is not necessarily separated. However, it can be said that the board of directors is in a position to supervise the execution of such business, since the execution of business is performed by a representative director, or a director delegated by the representative director, based on the decision of the board of directors. To that end, the board of directors will supervise the executive directors who are engaging in ESG issues. In this regard, according to the Corporate Governance Code, the board of directors is required to effectively supervise the allocation of management resources and the execution of business portfolio strategies in order to contribute to the sustainable growth of a company (Supplementary Principle 4–2 (2)).

With regard to a company with committees, it can be said that the supervisory function of the board of directors is clearer, because the function of management and supervision are separated between the executive officer who makes decisions on business execution, and the board of directors who supervise it.

3.3 What compensation or remuneration approaches are used to align incentives with respect to ESG?

According to the Practical Guidelines on Group Governance System (https://www.meti.go.jp/policy/economy/keiei_innovation/keizaihousei/pdf/groupguideline.pdf) (available only in Japanese language) published by the Ministry of Economy, Trade and Industry in 2019, non-financial factors such as customer and employee satisfaction can have a significant impact on corporate value. Therefore, it is pointed out that setting non-financial indicators related to ESG and SDGs as key performance indicators for incentive compensation is also effective for improving corporate value (page 115 of the aforementioned guidelines).

The Guidelines point out that it is necessary to disclose specific information on which index was used as a non-financial indicator and why it was selected.

The Executive Remuneration Guidelines Considering ESG and SDGs (https://www.bhrlawyers.org/_files/ugd/875934_d4929862cb674b3898ffcbe55bc6a009.pdf) (available only in Japanese language), formulated and published by the Business and Human Rights Lawyers Network in October 2021, stipulates principles such as ensuring objectivity and selecting indicators in accordance with ESG issues, in addition to disclosing the indicators.

3.4 What are some common examples of how companies have integrated ESG into their day-to-day operations?

There are various ways to incorporate ESG into daily business operations, including the following:

- including ESG clauses in various transaction agreements that oblige counterparties to comply with ESG standards and codes of conduct;
- identifying environmental and human rights issues and problems through due diligence in M&A transactions, and reflecting them in transaction terms and conditions;
- receiving and responding to reports regarding human rights, environmental and other ESG issues from stakeholders such as employees, business partners and customers in an extended internal reporting system;
- including indicators for ESG issues in subsidiary and supplier management; and
- conducting internal training regarding ESG issues.

3.5 How have boards and management adapted to address the need to oversee and manage ESG issues?

The boards and management of Japanese companies generally address ESG issues using the following methods:

- Establishing an internal sustainability committee and formulating a sustainability policy. According to Japan Spence Stuart Board Index (https://jp.spencerstuart.com/-/media/2024/02/2023-japan-board-index/ssbi_japan_board_index_2023_jp.pdf) (available only in Japanese language), about 87% of Nikkei Stock Average 225 and TOPIX100 companies have a sustainability committee or relevant organisations.
- Making ESG issues a key topic for dialogue in investor engagement.
- Disclosing the status of efforts to address ESG issues. With respect to the disclosure of ESG information, under the amended Cabinet Office Ordinance on Disclosure of Corporate Affairs, etc. in January 2023, it is required to disclose certain non-financial information, including ESG-related information in annual securities reports (see question 1.2).

4 Finance

4.1 To what extent do providers of debt and equity finance rely on internally or externally developed ESG ratings?

In general, ESG ratings has become very important in recent years. For example, Japan's Stewardship Code (https://www.fsa.go.jp/news/25/singi/20140227-2/05.pdf) clearly states that the content of stewardship responsibilities should take into account medium- to long-term sustainability, including ESG elements (page 5 of the Code).

In the Code of Conduct for ESG Assessment and Data Providers (https://www.fsa.go.jp/news/r4/singi/20221215/01.pdf) (available only in Japanese language) published by the FSA in 2022, the FSA pointed out that the use of ESG rating and data has expanded. It has been pointed out that in the context of institutional investors making investment decisions as well as in the context of engagement regarding ESG-related initiatives, this Code is widely referenced when selecting subjects for engagement and examining the content and methods of engagement (page 3 of the Code).

Companies also recognise the importance of ESG assessment. According to the results of the fourth Keidanren questionnaire on the Charter of Corporate Behaviour (https://www.keidanren.or.jp/policy/2018/059_kekka.pdf) (available only in Japanese language) companies also disclose ESG information for the purpose of responding to investors, and rating agencies.

However, while the importance of ESG rating has increased, there are indications that ratings of the same company vary widely among rating agencies, and there are indications that the validity and reliability of ratings have become questionable.

4.2 Do green bonds or social bonds play a significant role in the market?

According to the Ministry of the Environment, the number of Japanese companies issuing green bonds has been increasing year by year (https://greenfinanceportal.env.go.jp/en/bond/issuance_data/market_status.html, https://greenfinanceportal.env.go.jp/en/bond/issuance_data/issuance_list.html).

However, according to the Green Bond and Sustainability Link Bond Guidelines (https://www.env.go.jp/content/000128193.pdf) published by the Ministry of the Environment (hereinafter referred to as the FY 2022 Guidelines), although the number of green bond issuances is currently increasing, they are still at a development stage when compared to their status overseas. In order to achieve the goal of carbon neutrality by 2050 and the reduction of greenhouse gas emissions by 46% compared to 2013 by 2030, the introduction of a large amount of private finance is required, and the current situation is not sufficient (page 22 of the FY 2022 Guidelines).

At the same time, with the expansion of the global green bond market, there is growing concern about greenwashing, and the need to ensure the credibility of the green bond market has been pointed out (pages 22–23 of the FY 2022 Guidelines).

4.3 Do sustainability-linked bonds play a significant role in the market?

According to the Ministry of the Environment similar to green bonds, the number of sustainability-linked bonds issued by Japanese companies is increasing year by year (https://greenfinanceportal.env.go.jp/en/bond/slb_issuance_data/slb_market_status.html, https://greenfinanceportal.env.go.jp/en/bond/slb_issuance_data/slb_issuance_list.html).

The sustainability-linked bonds are funding instruments that can be used for general sustainability purposes, and serve to promote advanced sustainability management through sustainability performance targets (SPTs). They are expected to be used more as a means of enhancing sustainability management by companies in the future.

4.4 What are the major factors impacting the use of these types of financial instruments?

Since the Ministry of the Environment established the Green Bond Guidelines in 2017, the issuance price of green bonds by Japanese companies has been increasing year by year. In addition, the number of cases of green loans and sustainability-linked loans have increased since the announcement of the Principles for Green Loans in 2018 and the subsequent announcement of the Principles for Sustainability-Linked Loans in 2019. In response to this situation, the Ministry of the Environment announced the 2020 Green Bond Guidelines and the 2020 Green Loan and Sustainability-Linked Loans Guidelines, both revised versions of the 2017 Green Bond Guidelines, in March 2020, further increasing the number of cases of such financing methods.

The Sustainability-Linked Bond Principles were established in June 2020, and in response, the Ministry of the Environment released the FY 2022 Guidelines in July 2022, clarifying the criteria and ensuring the credibility of the market, which resulted in an expansion of the use cases.

In addition, the Ministry of the Environment provides subsidies to fund procurement supporters who support companies and local governments that seek to raise funds through green bonds (https://greenfinanceportal.env.go.jp/en/greenfinance/promotion_support/issuance_list.html), and these measures also contribute to the expansion of the examples of utilisation.

4.5 What is the assurance and verification process for green bonds? To what extent are these processes regulated?

According to the FY 2022 Guidelines, prior to issuing green bonds, it is desirable that they be reviewed by an external organisation in order to assess the suitability of the purpose of proceeds, the project evaluation and selection processes, the management of proceeds, and reporting (disclosure) (page 50 of the FY 2022 Guidelines).

In addition, after the issuance of green bonds, the latest information on the use of proceeds should be reported (disclosed) online at least once a year until all proceeds have been allocated (page 47 of the FY 2022 Guidelines).

Furthermore, after the issuance of green bonds, it is desirable that they be reviewed by outside auditors and other third parties on the management of proceeds in order to internally track and verify the use of proceeds for green projects (page 50 of the FY 2022 Guidelines). The results of reviews by outside organisations should be disclosed (page 52 of the FY 2022 Guidelines).

4.6 What other developments and factors are driving or hindering the financing of green projects?

As mentioned above, though concerns about green bonds have been raised by greenwashing, market reliability has been improved by the formulation and publication of the FY 2022 Guidelines.

In the context of transition finance, there is the issue of financed emissions (the issue that, when financial institutions make investments and loans, they are required to achieve net-zero emissions, including greenhouse gas emissions from the companies they invest in). In October 2023, the FSA published the document Addressing the Challenges of Financed Emissions (https://www.fsa.go.jp/singi/transition_finance/siryou/20231002/02.pdf), which indicates that it is necessary to clarify the criteria and policies for transition finance issues. The government and the private sector are considering this issue.

5 Trends

5.1 What are the material trends related to ESG?

As global concerns regarding climate change intensify, the significance of corporate engagement with ESG initiatives has become increasingly paramount. This evolving landscape is significantly influencing corporate practices in Japan, where regulatory frameworks and stakeholder expectations are rapidly adapting to ensure greater corporate accountability and sustainability.

Disclosure requirements

Starting from the fiscal year ending March 2023, Japanese annual securities reports are now mandated to include a new section dedicated to sustainability information. This requirement compels companies to enhance transparency regarding their environmental impacts and sustainability practices. A particularly noteworthy development is how the Financial Services Agency (FSA) is advancing discussions aimed at mandating the disclosure of greenhouse gas emissions. This initiative represents a significant shift in regulatory expectations, underscoring the urgency of climate action within the corporate sector. The FSA has proposed a phased approach to implementing this requirement, initially targeting companies listed on the Prime market of the Tokyo Stock Exchange, specifically those with a market capitalisation exceeding 3 trillion yen. The newly required disclosure standards will be based on the criteria published by the International Sustainability Standards Board (ISSB) in June 2023, which will then be incorporated into the standards finalised by the Japanese Sustainability Standards Board (SSBJ) by the end of March 2025. The draft of these standards outlines three categories of emissions, which are crucial for companies to monitor and disclose (https://www.ssb-j.jp/en/about.html):

- **Scope 1**: Direct emissions from the company's operational facilities.
- **Scope 2**: Indirect emissions resulting from energy consumption at these facilities.
- **Scope 3**: Emissions associated with procurement, manufacturing, and transportation activities.

This comprehensive approach not only addresses a company's direct environmental impact but also emphasises the importance of accountability throughout the supply chain. Companies listed on the Tokyo Stock Exchange with a market capitalisation exceeding 3 trillion yen are expected to be mandated to disclose Scope 3 emissions as early as the fiscal year ending March 2027, with plans for gradual expansion to additional companies. However, it is important to note that the establishment of internal systems for collecting data and calculating emissions remains inadequate. Currently, only 4% of companies have disclosed their Scope 3 emissions, indicating that progress in greenhouse gas emission disclosures is far from satisfactory.

Shareholder proposals

The landscape of shareholder engagement is also evolving. In June 2024, the number of companies responding to shareholder proposals is anticipated to reach a record high of 91, marking three consecutive years of increasing participation. This surge reflects a broader recognition of the critical role that corporate activities play in influencing environmental outcomes and the necessity for companies to adopt sustainable practices. In light of the heightened global focus on the impact of corporate activities on the environment, engagement with ESG initiatives is imperative. Shareholder proposals related to ESG continue to be robust, with some NGOs advocating that major banks and utility companies strengthen their responses to climate change. These proposals are becoming increasingly sophisticated, reflecting a growing awareness among shareholders of the potential risks and opportunities associated with climate change. Recent trends indicate a growing demand for disclosures concerning directors' competencies related to climate change risks and the status of lobbying efforts concerning decarbonisation policies. However, in general practice, it is common in Japan not to adopt shareholder proposals that are advisory in nature, thereby necessitating their linkage to matters requiring shareholder resolutions, such as amendments to the Articles of Incorporation. Moreover, according to Japanese *Companies Act*, a two-thirds majority vote is required to amend the Articles of Incorporation, presenting a significant hurdle for shareholders aiming to effect change. Therefore, it is crucial to recognise that in Japan, most environmental proposals require amendments to the Articles of Incorporation, which complicates their acceptance by companies. In 2023, the support rate for climate change-related proposals from NGOs was only about 20%, a decline from approximately 35% when such proposals were first introduced in 2020. This decline suggests a waning enthusiasm in the market regarding decarbonisation initiatives, potentially indicating a need for renewed engagement strategies and stakeholder education. However, the FSA has recently announced the "Action Program for Corporate Governance Reform 2024" (https://www.ssb-j.jp/en/about.html). This programme aims to ensure sustainable growth and long-term enhancement of corporate value, emphasising the need for effective initiatives. Furthermore, the manner in which companies engage in dialogue with their shareholders is currently in a transitional phase.

Guidelines on Human Rights

In March 2022, the Inter-Ministerial Committee on Policy Promotion for the Implementation of Japan's National Action Plan on Business and Human Rights was established to develop guidelines for respecting human rights within supply chains. Following extensive discussions and public comment procedures, the "Guidelines for Respecting Human Rights in Responsible Supply Chains" were published in September 2022. These Guidelines, presented in a soft-law format, require all companies operating in Japan to commit to respecting human rights, thereby aligning with international norms and expectations. The publication of practical reference materials by the Ministry in April 2023 serves as a crucial tool for companies navigating these guidelines (https://www.meti.go.jp/english/press/2023/0404_004.html). These materials provide guidance on implementing human rights considerations into business operations, ensuring that companies can effectively integrate these principles into their supply chains. As companies build upon these foundational guidelines, it is expected that the practices surrounding human rights respect will continue to evolve and be refined, leading to enhanced corporate accountability and ethical standards.

Concerns about greenwashing

While interest in ESG-related financial instrument is on the rise, there are growing global concerns regarding greenwashing – specifically, the apprehension that funds marketed as ESG-compliant may not perform as advertised. This phenomenon poses a significant challenge for investors seeking to align their portfolios with their values. Although an "anti-ESG" movement has yet to emerge in Japan, the FSA has proactively amended its comprehensive supervisory guidelines to address issues related to greenwashing. In March 2023, the FSA's amendments defined the scope of ESG investment trusts and established specific verification criteria for the disclosure of ESG-related information by public investment trusts, as well as for the operational frameworks of investment management companies (https://www.meti.go.jp/english/press/2023/0404_004.html). However, there remains considerable room for further clarification regarding the boundaries of what constitutes an ESG investment trust, suggesting opportunities for improvement to enhance the inflow of foreign investment into Japan's ESG market.

In summary, Japan must continue to closely monitor both the regulatory environment surrounding ESG and the broader implications of these developments. As the landscape evolves rapidly, the commitment to ESG initiatives will be essential for companies striving to maintain their competitiveness in an increasingly conscientious global market. The integration of sustainable practices into corporate strategies is not merely a compliance obligation; it is a strategic imperative that will shape the future of business in Japan and beyond. The increasing importance of transparency, accountability, and ethical governance will undoubtedly redefine the corporate landscape, compelling companies to prioritise sustainability and social responsibility as core tenets of their business models. As stakeholders become more informed and engaged, companies that proactively address ESG challenges will be better positioned to thrive in this new paradigm.

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