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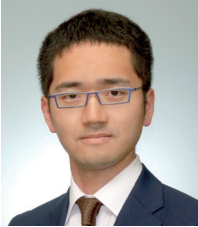
Standardization of sustainability disclosures so far and going forward in Japan

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Executive Summary



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Japanese companies are increasingly disclosing sustainability information. Greater understanding and utilization of sustainability information should lead to a more sustainable society in the future, including not only information standardized in compliance with Japanese and international disclosure standards but also narrative information that tells the story of a company's mission or essential value-add.

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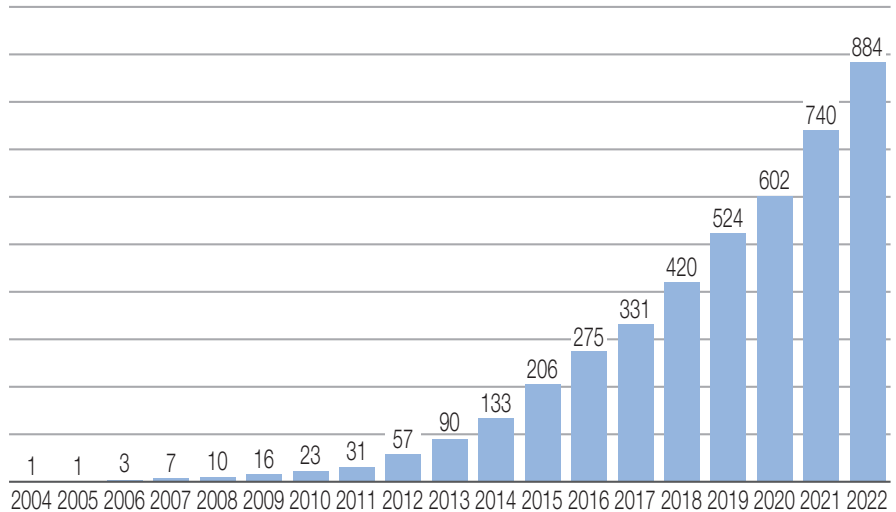
Challenges posed by sustainability disclosures' growing prevalence

Japanese companies have been ramping up environmentally and/or socially conscious sustainability activities since the Japanese government adopted a target of achieving carbon neutrality (net-zero greenhouse gas emissions) by 2050. They are disclosing information on their sustainability activities in a variety of formats, including sustainability reports and integrated reports. Financial institutions and other stakeholders are using sustainability information, together with financial information such as annual securities filings, for various purposes, including sustainable finance and screening of prospective investees.

In the wake of the ramp-up in corporate sustainability activities, companies that issue integrated reports or sustainability reports have been increasing year after year (Figure 1). These reports vary from company to company in terms of both how they are organized and what they are called, the latter of which includes "integrated report," "annual report" and eponymous titles. Where these reports reside on corporate websites likewise varies from company to company. Such variation poses a major challenge to users of sustainability information.

For example, when institutional investors such as asset managers and insurers engage with investee companies in the aim of adding value to the company, they often broadly gather and carefully analyze sustainability information published by the company. This information-gathering process is very time-consuming even in the current age of instant access to information. Institutional investors are concerned they will no longer have time to adequately analyze the information if the volume of sustainability disclosures maintains its recent growth trajectory.

Figure 1. Number of Japanese companies publishing integrated reports in Japanese



Source: Corporate Value Reporting Lab's 2022 report on trends in Japanese integrated reporting in support of sustained growth¹⁾

NOTE

1) To be counted as an integrated report by the Corporate Value Reporting Lab, a report must (1) explicitly state it is integrated report or (2) contain comprehensive financial and nonfinancial information and wording that implies it is intended as an integrated report (e.g., "report on corporate value creation").

While information vendors offer services to gather sustainability information, the metrics they use commonly differ from one vendor to another in terms of their, e.g., definition or unit of measure. Another issue is that such vendors' datasets often outdated or missing information due to inter-company differences in sustainability disclosures' timing. To verify that information is accurate, information users end up having to directly consult the integrated reports or sustainability reports that are the vendor's source documents, negating any gains in information-gathering efficiency that might have accrued from the vendor's services.

Standardization of disclosures in Japan and overseas

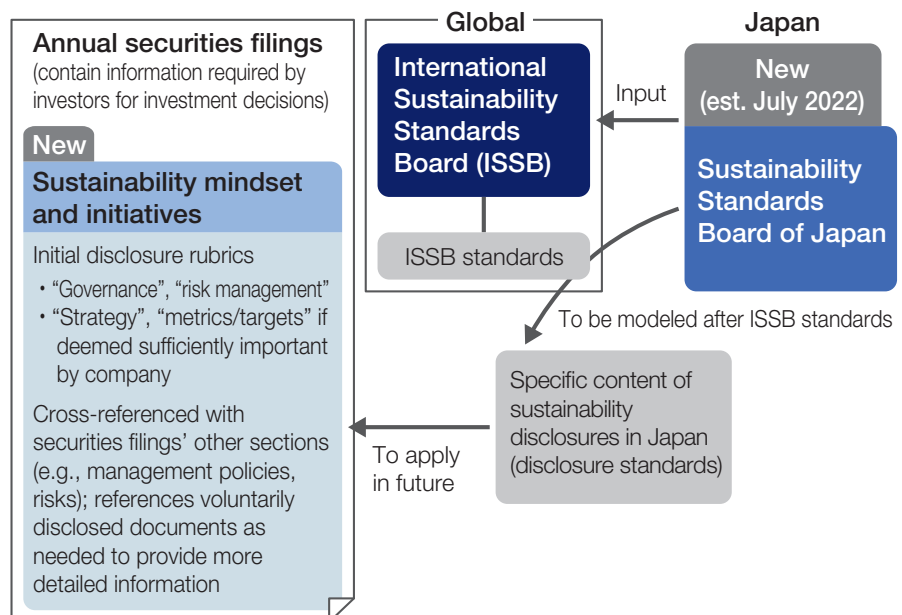
To resolve such issues, a movement to standardize sustainability disclosures is afoot globally. In Japan, the FSA released a draft amendment of a Cabinet Office Ordinance on corporate disclosures' content in November 2022. The amendment imposes new rules requiring certain sustainability information to be disclosed in annual securities filings. Specifically, the amendment requires the securities filings' company information to include a new section on the company's sustainability mindset and initiatives. Initially, the new section is required to contain disclosures under the rubrics of "governance" and "risk management" and may optionally include two additional rubrics, "strategy" and "metrics/targets", if deemed sufficiently important by the company. Under these new rules, publicly traded

companies have been successively disclosing the newly required information at their respective fiscal year-ends since March 31, 2023.

Internationally, the International Sustainability Standards Board (ISSB), the sustainability arm of the IFRS Foundation, the entity that sets International Financial Reporting Standards, issued the first two IFRS Sustainability Disclosure Standards, IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures, in June 2023. The ISSB standards incorporate the Task Force on Climate-related Financial Disclosures's recommendations as well as elements from multiple other pre-existing frameworks. They are intended to serve as a global baseline and a template for countries' respective national disclosure standards.

Japan is developing its own sustainability- and climate-related disclosure standards modeled after the ISSB standards. This effort is being spearheaded by the Sustainability Standards Board of Japan, which was established to provide Japanese input to ISSB standard-setting. The Japanese equivalents of IFRS S1 and S2 are slated to be released in draft form by March 31, 2024, and in final form during fiscal 2024. They are expected to eventually apply to the annual securities filings' sustainability disclosures.

Figure 2. Standardization of sustainability disclosures



Source: Excerpted from FSA presentation on amendment of Cabinet Office Ordinance on corporate disclosures

The future of disclosure standardization

Standardization of sustainability disclosures in Japan and overseas should facilitate inter-company comparative analysis and access to a wide variety of data while also driving diversification of sustainability information use cases. Meanwhile, companies will presumably continue to take the initiative to put out sustainability information that adeptly tells a story in the aim of emotionally resonating with stakeholders and gaining their understanding. Such stories may pertain to the company's mission or how the company creates essential value in pursuit of sustained growth.

Information users need to accurately understand and analyze such idiosyncratic narrative information in addition to standardized sustainability information. Even providers of information-gathering support services will have to comprehensively collect and provide both standardized and idiosyncratic narrative information on a timely basis, utilizing AI and other leading-edge technologies, to help information users form an accurate understanding.

Broadly disclosing and sharing sustainability information in easily understandable and user-friendly formats, promoting widespread use of the information and fostering accurate understanding across a broad spectrum of stakeholders should lead to a truly sustainable society in the future.

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