

# The JFSA's Strategy on Sustainable Finance (July 2021-June 2022)<sup>1</sup>

## Promoting sustainable finance<sup>2</sup>

As the world moves toward building a sustainable society, the importance of finance that could facilitate industrial and social transition is increasing. In particular, recognizing that the global trend is accelerated toward decarbonization, it is urgent to develop, in cooperation with market participants, a favorable environment for promoting sustainable finance that could attract capital for growth from home and abroad to the efforts of Japanese companies. In doing so, the JFSA will promote measures to ensure that corporate efforts are appropriately evaluated, including the efforts for transition in industry to achieve carbon neutrality.

### 1. Enhancement of corporate disclosure, both in quality and quantity

The JFSA will encourage companies listed on the Prime Market segment of the Tokyo Stock Exchange, which will open in April 2022, to enhance the quality and quantity of disclosure based on the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) or an equivalent framework based on the revision of the Corporate Governance Code in June 2021. In addition, in the Disclosure Working Group under the Financial System Council, the JFSA will discuss how listed companies and other companies that submit securities reports should appropriately disclose their sustainability-related initiatives to make Japanese market more attractive as an investment destination in the global context.

Both the public and private sectors will actively participate in the initiative to develop a comparable and consistent disclosure framework for sustainability, including climate change, by International Financial Reporting Standards (IFRS) Foundation.

### 2. Demonstration of market functions

In order to realize a "Green International Financial Center," it is essential to create an environment in which various domestic and foreign investors can easily and appropriately make investment decisions contributing to decarbonization.

To this end, in coordination with issuers and a wide range of other stakeholders, and based on the practices of institutional investors and other market participants, the JFSA works to

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<sup>1</sup> Excerpt from *The JFSA Strategic Priorities July 2021-June 2022*, Financial Services Agency, August 31, 2021.

<sup>2</sup> Sustainable finance: a type of finance intended to realize a sustainable society.

develop standards related to the use of proceeds and other elements, and aims to establish a framework for objectively confirming the eligibility of green bonds, etc. Furthermore, in cooperation with the Japan Exchange Group (JPX) etc., the JFSA will establish an information platform to broadly consolidate information on the confirmed green bonds etc., as well as the issuers' management and policies regarding ESG (Environmental, Social, and Governance).

The role of ESG rating organizations and data providers, as a bridge between enterprises and investors, is also important. In order to build an ecosystem where evaluations and data are used in a trustworthy manner, the JFSA plans to develop a code of conduct expected of ESG rating organizations and data providers regarding issues such as the transparency and comparability of evaluation methodologies as well as governance, with the aim of ensuring the independence and objectivity of evaluations. To this end, the JFSA will invite experts and other stakeholders to a panel for discussion, bearing in mind clarification of the roles to be played by enterprises and investors.

In addition, from the viewpoint of investor protection, the JFSA will monitor asset management companies and distributors regarding ESG-related investment trusts for individual investors, which are rapidly growing.

With regard to social bonds,<sup>3</sup> based on the new guidelines, the JFSA will consider formulating a document that provides specific examples of indicators regarding the social benefits of social projects in cooperation with relevant ministries and agencies.

### **3. Financial Institutions' support for the borrowers and investees, and climate change risk management**

Financial institutions are expected to be actively engaged with investment and loan recipients and to provide them with expertise and other support, so that they can address climate change. From the perspective of steadily promoting such efforts by financial institutions, the JFSA will further work on sharing information and knowledge for regional financial institutions to effectively engage in local companies' decarbonization.

It is also important for financial institutions to recognize that how to respond to climate change is a management challenge and to establish an appropriate preparedness for addressing it. Specifically, financial institutions are expected to establish a governance system for climate-related risks, develop business models and strategies that take into account the risks and opportunities of climate change, establish a process for recognizing, assessing and managing climate-related risks, and utilize scenario analysis.

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<sup>3</sup> Social bonds are bonds issued in order to raise funds for projects that contribute to the resolution of social challenges.

From these perspectives, in this business year, the JFSA, in collaboration with the Bank of Japan, will conduct a pilot exercise of scenario analysis using NGFS scenarios as common scenarios for three megabanks and three major non-life insurance groups. At the same time, the JFSA will clarify the monitoring viewpoints with regard to financial institutions' efforts to engage with investment and loan recipients and manage climate-related risks. The JFSA will develop those viewpoints for depository financial institutions and insurance companies as a first step.

#### **4. Active participation in international discussions**

Taking into account that COP26 (The 26th United Nations Climate Change Conference of the Parties) will be held in November 2021, the JFSA will play a leading role in international sustainability-related discussions on such matters as disclosure, smooth private capital mobilization, enhancement of capital market functions, and climate-related risk management. The JFSA will also accumulate knowledge on how considerations on data, metrics, and sustainability-related issues beyond climate change are evolving internationally in order to contribute to the domestic policy development.

In addition, the JFSA will keep abreast of discussions on international initiatives by the private financial sector in a timely manner, and consider frameworks to support financial institutions participating in such initiatives, while cooperating with such initiatives and utilizing the results of such discussions.

*The attached "Supplementary Document" comprehensively and concretely describes the JFSA's achievements in the last business year and its work plan for this business year to clarify the PDCA cycle of the JFSA' work.*

## **Supplement Document**

### **Promotion of sustainable finance**

Based on the "Report by the Expert Panel on Sustainable Finance" released in June 2021, the following measures will be promoted:

#### **1. Enhancement of corporate disclosure, both in quality and quantity**

##### **Achievements in the last business year**

- The revision of the Corporate Governance Code in June 2021 requires companies listed on the Prime Market to enhance the quality and quantity of disclosure based on the TCFD recommendations or an equivalent international framework.
- As part of our participation in the IFRS Foundation's initiatives to develop a sustainability-related reporting framework, the JFSA gathered the opinions of domestic private sector stakeholders and relevant ministries and agencies in response to the IFRS Foundation's public consultation on the establishment of a standard setting board for sustainability reporting, and submitted a comment letter as Japan's response. Japan also submitted a comment letter on the IFRS Foundation's proposals to amend its Constitution, including the membership of the new standard setting board.
- The Expert Panel on Sustainable Finance discussed aforementioned IFRS Foundation's initiatives and other trends on sustainability disclosure. The Panel compiled a report with recommendations, including the continued consideration of enhancing climate-related disclosure, while keeping a close eye on international trends.
- Through the TCFD Consortium and other organizations, the JFSA promoted voluntary efforts by the private sector to disclose information in line with the TCFD recommendations, such as by supporting the "TCFD Summit 2020" and the formulation of "TCFD Guidance 2.0." The JFSA also co-hosted the seminar on "TCFD Disclosure and Transition Finance" jointly with the JPX in April 2021.
- From the perspective of enhancing the disclosure of ESG information, including climate change, the JFSA published a report on good practice on the corporate disclosure of descriptive information, including ESG elements (November 2020).

##### **Work plan for this business year**

- Based on the revision of the Corporate Governance Code in June 2021, the JFSA will encourage listed companies to disclose their initiatives on sustainability. In particular, the revised Corporate Governance Code will require companies listed on the Prime Market to enhance the quality and quantity of disclosures based on the TCFD recommendations or

an equivalent international framework.

- In light of changes in the economic and social circumstances surrounding companies, the Disclosure Working Group of the Financial System Council will discuss the appropriate way to disclose sustainability efforts, while listening to the opinions of a wide range of stakeholders, in order to make the Japanese market more attractive as an investment destination in the global context.
- Japan will actively participate in the initiative to develop a comparable and consistent disclosure framework for sustainability, including climate change, by the IFRS Foundation, including the dissemination of opinions.
- The JFSA will revise the reports on good practices on sustainability-related disclosure with a view to enhancing the disclosure of ESG information, including climate change,
- The JFSA will support the promotion of dialogue between companies and investors in Japan on TCFD disclosure through activities such as the TCFD Consortium, and disseminate and promote Japan's initiatives as best practices internationally.

## **2. Demonstration of market functions**

### Achievements in the last business year

- The above-mentioned Expert Panel discussed how the capital market can demonstrate its function to contribute to the promotion of sustainable finance, and comprised the report with recommendations, including the establishment of a framework to objectively confirm the eligibility of ESG-related bonds and the development of a platform to provide practical information which is beneficial to enterprises and investors.
- In addition, the "Working Group on Social Bonds I" was established under the Panel. Based on the discussions at the Working Group, the JFSA compiled the draft social bonds guidelines.

### Work plan for this business year

- In order to realize a "Green International Financial Center" where Green Bonds, etc. are actively traded, the JFSA, in cooperation with a wide range of stakeholders including issuers, will develop standards based on the practices of institutional investors and aim to establish a framework to objectively confirm the eligibility of Green Bonds, etc., including criteria for use of proceeds. In addition, in cooperation with JPX and other organizations, the JFSA will develop an information platform, which would broadly consolidate information on the confirmed green bonds and issuers' management and

policies regarding ESG (Environmental, Social and Governance), as well as practical guidance for issuers and investors.

- In order to build an ecosystem where evaluations and data are used in a trustworthy manner, the JFSA plans to develop a code of conduct for ESG rating organizations and data providers, which serve as a bridge between companies and investors, regarding issues such as the transparency and comparability of evaluation methodologies as well as governance, with the aim of ensuring the independence and objectivity of evaluations. To this end, the JFSA will invite experts and other stakeholders to a panel for discussion, bearing in mind clarifying the roles to be played by enterprises and investors.
- From the perspective that it is important to carefully explain product characteristics to customers when creating and selling ESG-related investment trusts, and to continuously explain the status of the selected issues afterwards, the JFSA will conduct a wide range of research and analysis on the state of ESG and SDGs in the asset management industry, including specific indicators, and promote the monitoring of asset managers.
- In addition, in order to promote effective dialogue between institutional investors or financial institutions and enterprises, the JFSA will consider a framework to support financial institutions in participating in international initiatives by private financial sectors, which aims to facilitate decarbonization of enterprises.
- In order to ensure international credibility and transparency of transition, the JFSA will collaborate with relevant ministries and agencies on sectoral roadmaps to be formulated for the transition to decarbonization.
- With regard to social bonds, the guidelines will be finalized based on the results of the public comments on the draft version. After finalizing the guidelines, the JFSA will facilitate further discussions among related parties to provide specific examples of indicators for the social benefits of social projects.

### **3. Financial Institutions' support for the borrowers and investees, and climate change risk management**

#### Achievements in the last business year

- The JFSA took stock of the efforts and issues related to climate change by large financial institutions.
- The Expert Panel discussed the status of large financial institutions' addressing climate-related risks found through the aforementioned stock-taking, and compiled a report with recommendations, including the development of guidance on financial intuitions with a view to promoting their efforts on engaging with investment and loan recipients in their

efforts to address climate change and on the establishment of a climate-related risk management system.

- Based on these recommendations, a pilot exercise of scenario analysis based on a common scenario was launched for the three megabanks and three major non-life insurance groups in cooperation with the Bank of Japan. In the pilot project, the JFSA have discussed with the financial institutions the limitations of the data and the characteristics of the various methods, and reached agreement on the framework of scenario analysis which the JFSA ask them to conduct.
- In March 2021, the JFSA and the Ministry of the Environment launched the "Collaboration Team for Revitalizing Sustainable Regional Economies and Societies" with the aim of enhancing partnerships with parties that contribute to solving regional issues and supporting the efforts of regional financial institutions.

#### Work plan for this business year

- From the perspective of steadily promoting efforts by financial institutions to engage with their investment and loan recipients by providing expertise through active engagement to help them addressing climate change, the JFSA will further work on sharing information and knowledge with regional financial institutions so that they could effectively engage in the decarbonization of local businesses.
- The JFSA continues to conduct a pilot exercise of scenario analysis using NGFS scenarios as common scenarios for the three megabanks and the three major non-life insurance groups, in cooperation with the Bank of Japan, in order to encourage financial institutions to recognize that responding to climate change is a management challenge and to build an appropriate preparedness for addressing it. In particular, based on the scenario analysis framework agreed with the financial institutions in the last business year, the JFSA will discuss with financial institutions the results of the scenario analysis to identify issues that needs to be addressed in order to utilize the scenario analysis on measuring climate-related risks and developing their businesses and financial strategies, as well as on engaging in their investment and loan recipients.
- In addition, by around March 2022, the JFSA will clarify monitoring viewpoints on the internal systems necessary in the financial institutions to ensure appropriate climate-related risk management and to support investment and loan recipients to response climate change through active engagement. The JFSA will formulate those viewpoints on deposit-taking financial institutions and insurance companies as a first step.
- From the perspective of promoting the sustainable growth of regional economies, the JFSA, in cooperation with relevant ministries and agencies, will support efforts of regional

financial institutions to build businesses that utilize regional resources and solve regional problems by providing information to and sharing expertise with them.

- To support financial institutions' efforts to engage with investment and loan recipients, the JFSA will collaborate with the Ministry of Environment to conduct a project to support trial efforts by financial institutions to identify, calculate, and analyze the greenhouse gas emissions of their clients, and to identify the issues involved in such identification and analysis.

#### **4. Active participation in international discussions**

##### Achievements in the last business year

- In anticipation of the COP26 (The 26<sup>th</sup> United Nations Climate Change Conference of the Parties) to be held in November 2021, the JFSA has participated in discussions related to climate change at the G7 and G20 meetings, and at the G7 meeting in June 2021, the JFSA agreed to move toward mandatory disclosure based on TCFD framework, in line with domestic regulatory frameworks.
- At the NGFS, the JFSA has been elected as a new member of the Steering Committee and through these efforts, the JFSA has strengthened collaboration among relevant authorities.
- The JFSA has also contributed to discussions on addressing sustainability risks, particularly climate change, at the FSB and other standard setters. The officials of the JFSA have co-chaired relevant working groups at the FSB and IOSCO.
- In November 2020, the JFSA participated in the IPSF and has since contributed to international discussions by co-chairing the working group on disclosure.

##### Work plan for this business year

- Keeping in mind that COP26 will be held in November 2021, the JFSA will play a leading role in international discussions on disclosure, smooth mobilization of private capital, enhancement of capital market functions, and climate-related risk management at the NGFS, FSB, IOSCO, IPSF, etc.
- The JFSA will also keep abreast of discussions on international initiatives by the private sector to support corporate decarbonization, and consider frameworks to support financial institutions' participation, while cooperating with such initiatives and utilizing the results of discussions.
- In preparation for international movements to develop data and metrics for measuring climate-related risks and structuring ESG-related products, the JFSA will study the status

and accuracy of relevant data in Japan and overseas.

- The JFSA will accumulate knowledge on sustainability-related issues beyond climate change, such as biodiversity, for which international efforts are already underway, and consider how to contribute to domestic policy developments.