



ESG Disclosure Study Group Report 2023

-Achieving World-Leading Disclosure and Dialogue Standards-

Executive Summary

June 2023

ESG Disclosure Study Group / EDSG

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1. About the ESG Disclosure Study Group

Name	ESG Disclosure Study Group / EDSG
Established	June 15, 2020
Vision	We will create a system that will harmonize the sustainable development of society with companies' increase in their own value and growth.
Major activities	<ul style="list-style-type: none">(1) Exploring effective and efficient ESG information disclosure frameworks(2) Accumulating practical examples (demonstrations) related to ESG information disclosure(3) Promoting mutual understanding among stakeholders for better decision-making(4) Publishing reports on research results(5) Businesses incidental or related to each of the preceding items, which are required for achieving the purposes of EDSG
Representative Director and Study Group Chair	Tetsuo Kitagawa, Ph.D. (Emeritus Professor of Aoyama Gakuin University and Professor at Tokyo Metropolitan University)
Membership (As of the end of May 2023)	122 companies and 11 organizations
Web	https://edsg.org

2. Suggestions

Based on the findings from the activities of the third term, we propose a better way of ESG information disclosure compiled by the study group.

Position of Suggestions

- The ESG Disclosure Study Group has since its establishment in June 2020 been committed to its mission of creating a mechanism for harmonizing the continuous development of society with corporate efforts to increase their value and to achieve growth. We have discussed the current state of non-financial information disclosure and problems with it in hopes that it will be beneficial to both companies and investors.
- In June 2022, we developed separate suggestions to issuers, investors, and standardizing bodies with regard to the achievements for two years, what the ESG information disclosure should be like based on the achievements, and what more effective dialogues between issuers and investors would look like. They were published in Japan and overseas in form of activity reports.*
* [ESG Disclosure Study Group Report 2022 – Achieving World-Leading Disclosure and Dialogue Standards](#)–, and [Executive Summary of Activity Reporting](#)
- The previous activity report presented suggestions that reflected the fundamental ideas of the Study Group. They are still effective and practical, in view of changes in the external environment, such as Japanese and overseas trends towards instituting laws, regulations and standards for non-financial information disclosure, progress in corporate disclosure, and the state of use of non-financial information by investors.
- During the term in question, the members studied the prescribed performance and improvised performance in the integrated report as a significant means that allows businesses to publish their long-term value creation (LTVC) stories on the subject of human capital disclosure, which is now in growing demand, and discussed a desirable form of dialogue between companies and investors, using the previous suggestions as a basis of our studies and discussions.
- The suggestions in this report have been created on the basis of subject matters in members' discussions about the achievements of activities in the twelve-month period from July 2022 to June 2023.

2. Suggestions

Assumptions

- Behind the shift towards the obligation and standardization of non-financial information disclosure, there are investor needs for information that allows them to examine if companies can achieve the LTVC.
- Essentially, companies' response to regulations does not conflict with the LTVC. Corporate management executives are required to increase corporate value in consideration of the balance between financial and non-financial aspects. In this event, it is necessary to review the state of sustainability management from a viewpoint of disclosure.
- The ESG Disclosure Study Group has as its members companies that actively practice sustainability management, including non-financial information disclosure, and investors, to explore ideal visions of disclosure and dialogues.
- The primary purpose of these suggestions is to propose an approach for further improvement to companies already fully working for ESG information disclosure as well as to investors. I hope that they will also serve as a practical guide for companies that will start making ESG information disclosure.

2. Suggestions

(1) Basic Stance on Disclosure

Companies should not define the disclosure of compulsory or standardized items itself as an objective. The point is how non-financial information of a company leads to its LTVC. Integrated reports are a key means of communicating this.

- The scope of non-financial information subject to disclosure is enlarged in line with the introduction of obligations and standards. Today, the disclosure of more specific information, both qualitative and quantitative, is required. It is inevitable to comply with the obligations and standards introduced. However, it should not be regarded as an objective.
- With regard to non-financial items important to the LTVC, it is vital to select them in consideration of the path via which they impact financial matters, and to explain the ideas and conditions behind the selection, indicators, and medium- and long-term targets.
- For this purpose, first, management executives need to recognize that non-financial factors are involved in the procurement and construction of management resources and to manage them. Then, in consideration of their companies' material issues, they should identify which non-financial information is important and endeavor to create value. These are the roles of business managers.
- Companies can exhibit their essential originality by expressing their stories of value creation devised with the close involvement of management executives in conjunction with non-financial factors and intangible assets, such as technological strengths that generate their competitiveness and personnel capabilities. Integrated reports are a key means of communicating this.

2. Suggestions

(2) Compliance with Regulations

Companies are required to build their optimal implementation structure by monitoring the latest trends on the introduction of obligations and standards for non-financial information disclosure and on the basis of an analysis of any disparity with their status quo.

- The introduction of obligations and standards for non-financial information disclosure is making rapid progress in Japan and overseas. That requires companies to understand what new complicated regulations and standards demand and to meet them in a timely manner. Meanwhile, quite a few companies are facing issues such as the growing burden on disclosure personnel and the limited number of human resources holding expertise.
- Companies are urgently required to take actions for non-financial information disclosure. To take timely action, they need to train internal personnel to have the necessary knowledge and study employing outside experts and tools to understand the latest trends in non-financial information disclosure and for collecting and analyzing data including those about supply chains.
- Corporate managers should understand issues on resources involved in non-financial information disclosure and endeavor to construct an efficient and effective implementation structure.

2. Suggestions

(3) Connectivity Between Non-financial and Financial Information

Companies should explain the relationship between their non-financial efforts and their LTVC in a visualized form.

- The impacts of corporate non-financial efforts on financial affairs are attracting rapidly growing interest.
- From the perspective of connectivity between non-financial and financial information in information disclosure, it is important to visualize how non-financial efforts, including human capital, leads to the LTVC in their corporate strategies with the use of impact path, logic tree and other methods, and then to explain it. In this event, it is also helpful to give integrated presentations about related indicators, such as employee engagement, turnover ratio, and other indicators of loyalty when discussing human capital.
- As for quantification initiatives, various earlier examples in Japan and overseas are reported, including those in the academic area. An analysis made by a subcommittee of the Study Group has confirmed that data related to human capital, such as investments in human capital and personnel measures, has some impact on financial figures through employee engagement.
- Companies should judge if they need to perform an independent quantitative analysis and to disclose it in view of earlier examples in Japan and overseas.

2. Suggestions

(4) Connectivity Between Non-financial and Financial Information in human Capital Disclosure

Companies should develop personnel strategies for achieving the LTVC, identify disclosure items in terms of human capital that are important to management strategies, and explain target settings and the thinking behind them.

- Disclosure of human capital is now in rapidly increasing demand. It is the integration of management strategies with personnel ones that should be considered as a prerequisite.
- It is significant that companies make clear for the achievement of the LTVC in their personnel strategies how human capital links to the LTVC, including in cases where business model reforms are needed, what kinds of personnel (personnel portfolios) are needed, and how such personnel will be acquired and retained (through recruitment and development) and establish a common view shared across the organization from the management team to working-level personnel.
- The Guidelines for Human Capital Visualization presents 19 items, such as personnel development and diversity, as examples of disclosure items concerned with human capital. Companies should explain in their integrated reports and other disclosure media how their indicators and actions are associated with their management strategies.
- Teamwork, which is generated by strategically combining capabilities of individual employees, will also provide strength for the human capital. To display the performance of teamwork, it is necessary not only to disclose individual items but also to give complex explanations about them.

2. Suggestions

(5) Effective and Efficient Selection of Multiple Disclosure Media

Companies should make their own decisions on the selection of media for disclosing non-financial information on the basis of understanding both what information they want to convey and what investors want to know.

- Essentially, companies should decide at their discretion in which of their media they publish their non-financial information. It is also necessary to give consideration to the swift accessibility to investors of the information they seek, which is requisite to their investment decisions and evaluation.
- Integrated reports are an important means by which investors assess the feasibility of companies' LTVC. They should closely explain the stories of value creation and the key non-financial information associated with them. Companies should select ESG-related information and other details, including the way of linking them to websites, at their own discretion.
- This also goes for how to report financial information in integrated reports. While connectivity between financial and non-financial information is significant, arguments are split on whether or not financial information should be acquired from integrated reports. Some say that it is reader-friendly to include summaries of the balance sheet, the profit-and-loss statement, and cash flow statements in a single integrated report.
- It is significant for companies to see integrated reports as a space for an improvised performance that exhibits their value creation and to improve them with a reference to good examples of companies in other sectors as well as those of competitors.

2. Suggestions

(6) Expectations of Investors and Companies in Dialogues

Companies and investors should be more conscious of the viewpoint of intensifying the mutual understanding and interactivity of dialogues to prevent the dialogues themselves from becoming an objective.

- Investors should gain information offered by a company through integrated reports and other materials and develop hypotheses and their own views on the company's value creation process in preparation for a dialogue with it. Continued attempts to eliminate disparities in the company's disclosure information and investors' hypotheses and their own views will help deepen mutual understanding.
- It is vital for investors to understand the aspiration of companies to accurately understand investors' needs and interests and not to neglect to prepare to give plain explanations when requested to do so by companies.
- Investors have a range of management approaches. Depending on that, the specific disclosure items they pay attention to vary. Companies sometimes need to take positive actions, such as asking questions of investors, instead of merely passively responding to investors' questions in dialogues. When they honestly ask investors questions, for example, about their criteria for investment decisions, the relationship between the criteria and their questions in dialogues, and points which they find insufficient with respect to disclosure and dialogues on the company side, they will be able to understand investors' intent in dialogues. That will lead to a qualitative improvement in the dialogues.

2. Suggestions

(7) Expectations Regulatory Authorities and Standardizing Bodies

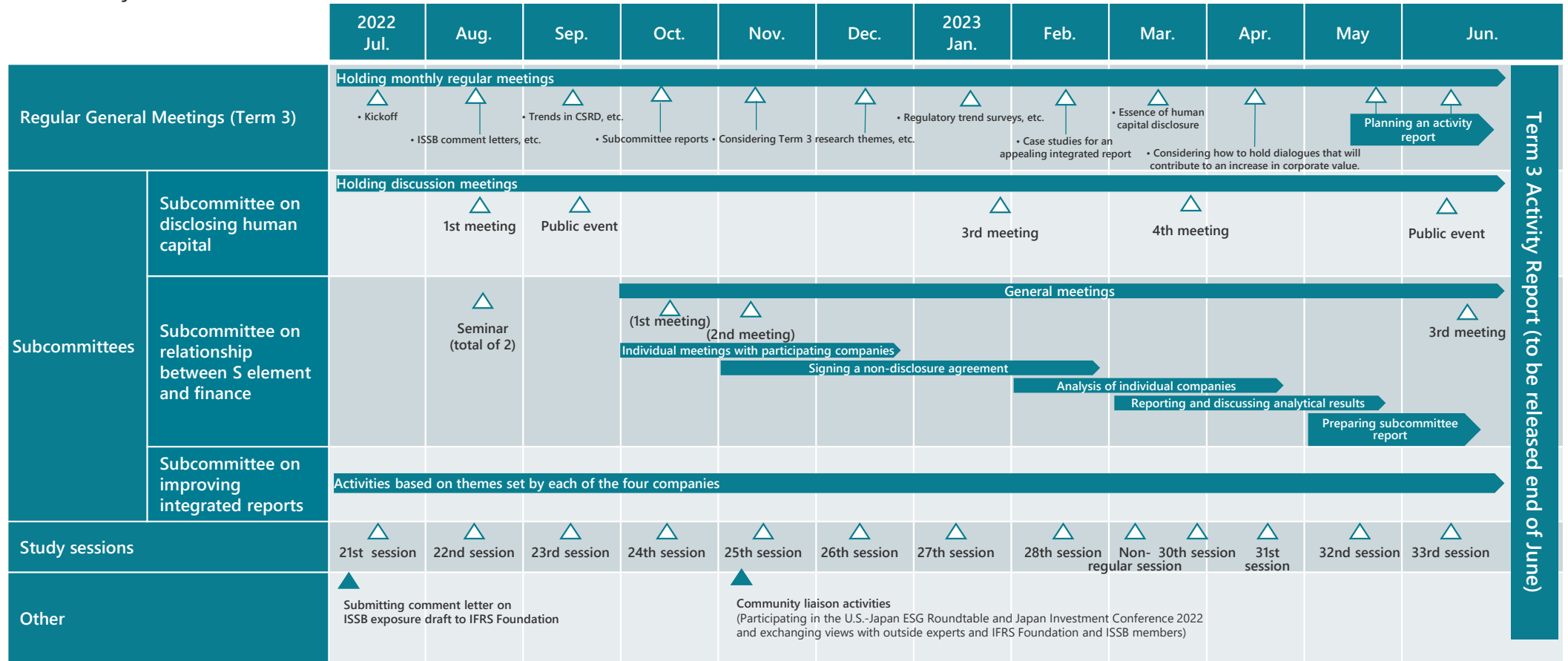
In terms of developing standards for non-financial information disclosure, it is hoped that interoperability will be increased through a collaboration among international standardization bodies, regulatory authorities in different countries and regions, and equivalent entities.

- If indicators and stances behind the regulations and standards for non-financial information disclosure vary with the country or region, it will be difficult for companies operating globally to grasp disclosure items relevant to their overall groups. In addition, it will be more difficult for investors using such information to make international comparisons.
- To ensure convenience in the disclosure and utilization of non-financial information, we hope that international standardization bodies and regulatory authorities in different countries and regions will continue their efforts to increase the interoperability of non-financial information disclosure standards and to ensure the transparency of ESG evaluation standards while focusing on the balance between globalization and localization.
- We also request that regulatory authorities in different countries and regions take action to ease the heavy burden on companies for meeting regulations in different areas in cases where they have subsidiaries in separate jurisdictions, for instance with the introduction of transitional measures.
- We communicated our stance through our comment letter in July 2022 and discussions to the ISSB, which was working to develop standards to serve as a global baseline. We welcome the ISSB's final draft, because it shares the same orientation with us in the sense that it is not rule-based but principle-based and that it defines human capital as a priority for the future.

3. Overview of Activities Conducted

• Background of Term 3 Activities

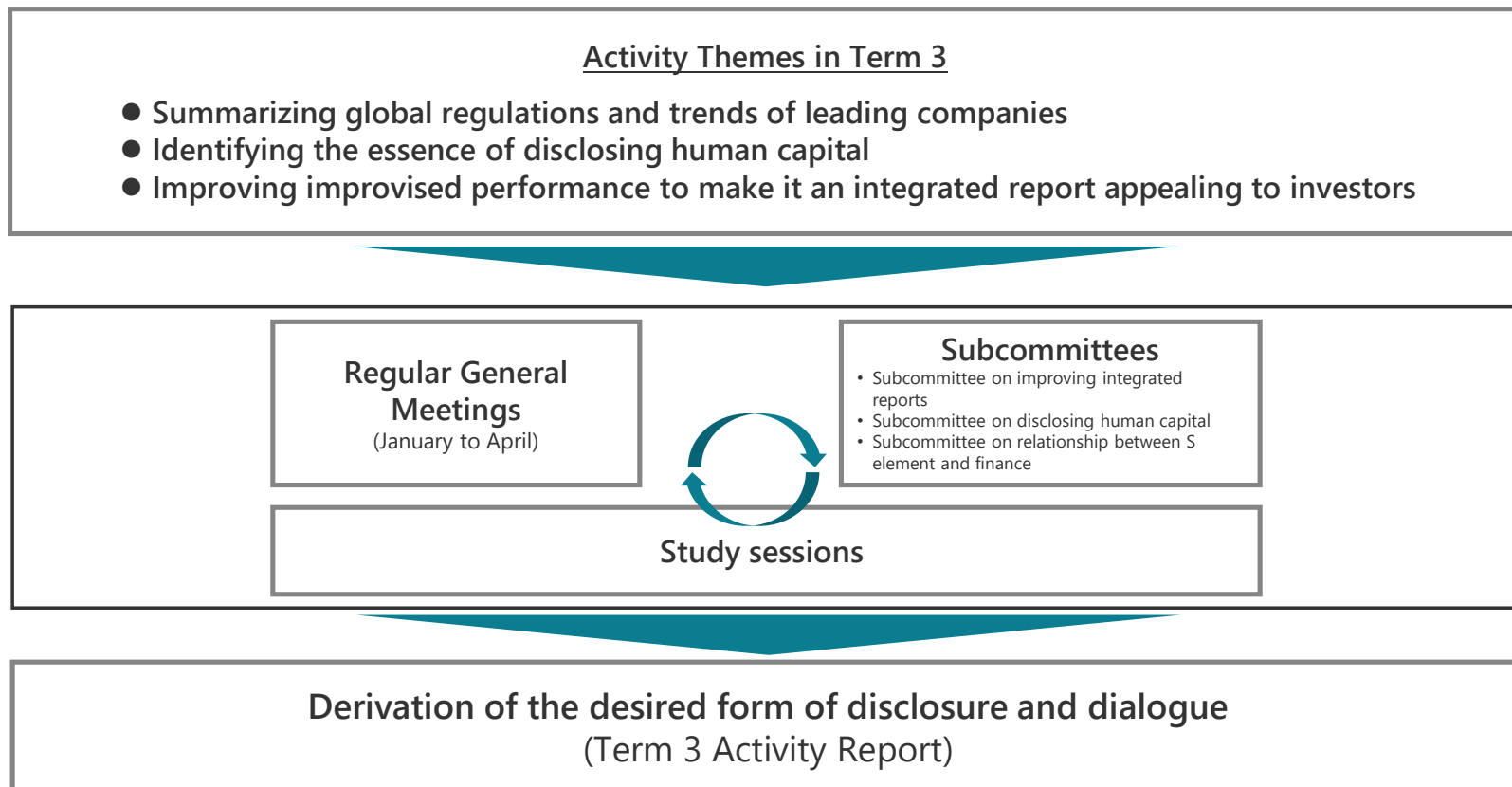
To explore the desirable form of disclosure, we monitored global trends and considered specific methods of improved performance on the themes of human capital through activities such as regular general meetings, subcommittee meetings, and study sessions in term 3.



3. Overview of Activities Conducted

- Approach to Term 3 Activities

In Terms 1 and 2, we organized our basic ideas of ESG information disclosure with the cooperation of members in various positions and compiled them in the form of an activity report. In Term 3, we explored specific methods of disclosing ESG information based on the report, focusing on the nature of improvised performance in the integrated report.



3-1. Desirable State of Disclosure

• Response to Japanese and Overseas Regulations for Non-financial Information Disclosure

We reported the results of the survey on Japanese and overseas regulatory trends and identified issues and required responses through the members' discussions and a survey.

Recognition of existing issues

- The trend toward mandatory and standardized disclosure of non-financial information is irreversible and accelerating.
- There are concerns that the burden of responding to items that will be mandated and standardized (prescribed performance) will increase, and value creation stories (improvised performance) will be diluted.
- In view of corporate valuation, the emphasis on the connectivity of financial and non-financial information and stories leading to purpose, vision, business strategy, and value creation remain unchanged.

Investigate trends in Japanese and overseas regulations for non-financial information disclosure (IFRS/ISSSB, US SEC, EU CSRD/ESRS, Japan)

Discussion and survey by members

Responses required to the development of tighter regulations and standards both domestically and internationally

- Issuer
- Acknowledge the latest trends and analyze the gap from the current status of their companies.
 - Secure resources and develop and build a promotion system based on the above (in-house production and use of external resources).
- Institutional investors
- Effective and efficient use of disclosed information (selection of necessary information)
- Issuers and institutional investors
- Foster a common understanding of the essence required for effective disclosure and evaluation through constant dialogue between issuers and institutional investors.
 - Elaborate methods for evaluating financial and non-financial information connectivity

3-1. Desirable State of Disclosure

• Presentation of Originality in Integrated Report

Members discussed and conducted a questionnaire on improvised performance in the integrated report from the viewpoint of originality, using examples of disclosure in Japan and overseas as a reference. Together with the results of the activities of the subcommittee on improving integrated reports, we identified the essence required of an integrated report that contributes to investors' investment decisions.

Recognition of existing issues

- The management’s message and value creation story are common sections that issuers want to be read and that institutional investors also want to read to know about the "uniqueness" of the company.
- Institutional investors recognize **materiality** as an important element in deciphering a company's character.
- Conscious of storytelling, introduction of specific initiatives, differentiation from other companies, etc. with the reader in mind
- Issues such as employee involvement and penetration, lack of quantitative information, and separation of disclosed information by media

The analysis of Nissin Foods Holdings Value Report and comparative analysis of Japanese, European, and U.S. reports

Discussion and survey by members

Outcomes of activities of the subcommittee on improving integrated reports

Elements necessary for portraying originality in integrated report

- | | |
|--|---|
| <ol style="list-style-type: none"> 1. Value creation story <ul style="list-style-type: none"> ● Develop a systematic story throughout the report (a story that connects purpose, vision, and business strategy) 2. Message <ul style="list-style-type: none"> ● Management leadership message: Confirm strategies and policies ● Messages from outside directors: Ensure the effectiveness of strategies and governance | <ol style="list-style-type: none"> 3. Expression of the company's identity <ul style="list-style-type: none"> ● Business model (product differentiation, positioning within the industry) ● External elements such as design (branding and expression of corporate climate/culture) 4. Information connectivity <ul style="list-style-type: none"> ● Relevance and connection among information posted in multiple disclosure mediums ● Disclosure of information in each medium with the intended audience in mind |
|--|---|

3-1. Desirable State of Disclosure

- **Discussions on Desirable Forms of Dialogues**

We discussed the desired form of dialogues between issuers and institutional investors that contributes to an increase in corporate value. Members raised opinions about challenges and innovations in raising corporate value through dialogues between issuers and institutional investors based on effective disclosure, with the results applied by issuers to their strategies and policies and by institutional investors to their corporate evaluations and investment decisions.



Attitudes toward dialogues

- **Bidirectional dialogues** are important. Companies need to be actively, not passively, involved.
- It is important **that** both parties **are aware of the purpose**. It is also useful to confirm the purpose of the dialogue in advance.
- It is necessary for companies to **provide** not only short-term plans, but also **a good medium- to long-term explanation** of the industry.
- **In dialogue with outside directors**, it is necessary to select (outside directors) in line with the agenda.

Purpose of dialogue

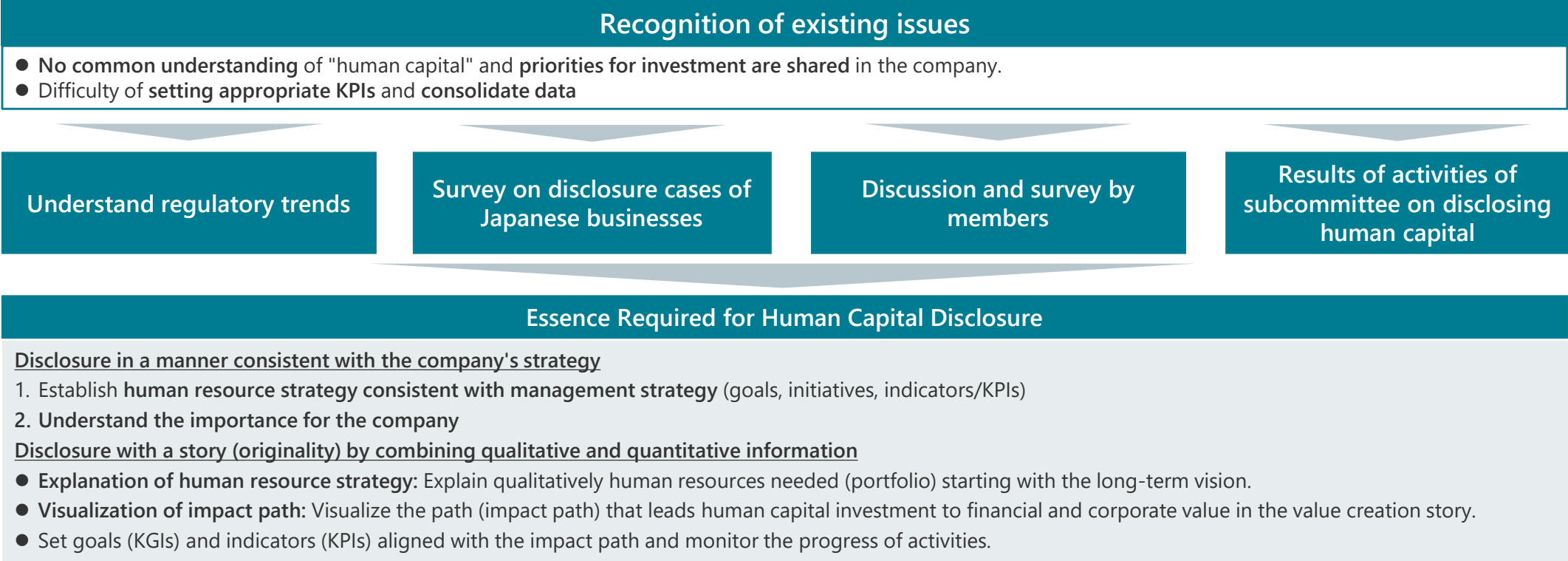
- Through dialogue, **information asymmetries** between issuers and investors **are eliminated**, leading to **agency cost reduction**.
- Investors **have different objectives for dialogue depending on their attributes**.

Feedback on dialogues

- While it is not necessary to accept all opinions in the dialogues, how they are actually incorporated into internal actions is important.
- There is a lead department for each issue and theme, and it is useful to provide feedback on requests, etc. as appropriate and examine them as necessary.

3-2. Specific Manners of Disclosure on Human Capital

With regard to human capital disclosure, which has been increasingly requested in recent years, we conducted a survey of global and Japanese regulatory trends and examples of domestic disclosure, and based on the input, conducted a discussion and questionnaire survey among members. Furthermore, based on the results of examination by the subcommittee on disclosing human capital, we have derived the essence of what is required for human capital disclosure from the perspective of improved performance.



3-3. Connectivity Between Non-Financial and Financial Information

While progress has been made in information disclosure and collection, such as non-financial sustainability information disclosure in securities reports, the subcommittee on the relationship between the S element and financial figures analyzed the relationship among employee engagement, human capital investment, and financial figures, and identified the following current status and issues.

Human capital-related data	▶ The combination of wage gap between men and women and the ratio of women in management positions, the combination of training expenses and the number of employees, and the ratio of adopting telecommuting affect financial figures.
Employee engagement	▶ Higher levels of satisfaction with the company (workplace satisfaction), satisfaction with human resource development measures, trust in the organization, evaluation of organizational management, and satisfaction with one's own work are associated with a stronger financial performance.

- ▶ **Human capital-related data (human capital investment and HR policies) affect financial figures through employee engagement.**
 - ▶ Groups with higher female managers: stronger financial performance through satisfaction with the company's human resource development and self-satisfaction with their work.
 - ▶ Groups with less overtime work and higher parental leave taken: stronger financial performance through trust in the organization and satisfaction with growth opportunities

Some relationships between employee engagement, human capital investment, and financial figures are **simple**, while others are **complex**, involving mediating variables and interaction effects (combinations of variables).

Need to analyze with appropriate combinations of various methods

- ✓ Understanding and applying statistical methods in the social sciences is desirable.
- ✓ Joint analysis with a university or outside research institutions if such personnel are not available in the company or department (NDA is required).

Issues recognized

Subcommittee implemented an approach of using data analysis to test hypotheses and improve measures.

- It is important to have a hypothesis (story) about the relationship between human capital investment, employee engagement, and financial figures.
- Reaffirming that it takes time and effort to comprehensively collect and organize data of varying granularity and jurisdiction
- It is also necessary to develop human resources, who will perform data analysis in-house

Will open a course on "ESG Sustainability Management and Data Analysis" to resolve issues identified at the Subcommittee

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