Principles for Financial Action towards a Sustainable Society

(Principles for Financial Action for the 21st Century)

The Drafting Committee for Environmental Finance Principles

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Foreword

The unforgiving earthquake and tsunami hit eastern Japan on 11 March 2011 cruelly exposed the powerlessness of man in the face of natural disasters. But it also shocked those of us who saw in it evidence that the scientific technologies supporting our day-to-day activities can suddenly disappoint our society. Witnessing the fragility of our civilized society through this so-called “March 11th” incident, we were all asked to revisit the meaning of sustainability.

Turning to issues on a global scale, there is indeed concern that in the future climate change and the loss of biodiversity, amongst other issues, may cause incommensurable damage. These problems come in addition to, other daunting issues, such as poverty and the heightened risks of an increased spreading of diseases (especially in developing countries) that intensify existing threats to human security. We must therefore aggressively tackle these global issues as we reconstruct Japan from the earthquake.

By rising to the challenges facing both Japan and the world, we can reach a platform from which further progress can be built on. If the post-earthquake reconstruction can trigger the sustainable use of energy or encourage us to design communities that respect ecosystems, these experiences may present a model social system for the 21st century. Herein lies the key to how finance can continue to be reliable and be trusted by society. We see the new role of finance in the 21st century as taking action towards the formation of a sustainable society.

Preamble

We understand the basics of a sustainable society as being able to live today free from the fear of tomorrow. In order for this to occur, this generation must seek to solve the various issues faced by humans and our planet - not only for our own benefit but also for future generations - by pursuing an environmentally friendly lifestyle that coexists with nature.

A fundamental part of society is the economic activity which involves a monetary intermediary. In order to steer society towards sustainability, we need to change the flow of money to those activities which correspond to such sustainability goals. This would mean directing money where society most needs it, which subsequently is the fundamental role of finance as it contributes to the development of society. In other words, by offering diverse financial services, it is thought that “the sustainability of society increases as a result of the most appropriate distribution of various resources between economic agents, regions and generations”.

The financial services industry’s cooperative action to finding solutions for global problems originates from the formation of the United Nations Environment Programme’s Finance Initiative in 1992. Since then, UNEP FI’s activities have expanded from environmental issues to social and governance issues, so called “ESG issues”. One of the Initiative’s outputs has been the establishment of the Principles for Responsible Investment (PRI) in 2006. As a separate programme facilitated by the International Finance Cooperation (IFC), the Equator Principles were launched in 2003 to manage environmental and social risks in project finance. The impetus of society for the financial services sector is for these initiatives to be translated into concrete actions and to accelerate the overall pace of change. How then should the financial services sector in Japan respond to these global demands? This should be addressed bearing in mind the significant responsibility it carries as the finance arm of one of the largest economies.

The Japanese financial services sector has two main roles. The first is to contribute to transforming Japan into a sustainable society. This requires not only to secure the safety of vital infrastructure against natural disasters, but also to support local communities and national industries in improving their sustainability and strengthening their competitiveness. The second role is to contribute to increasing sustainability as a global citizen. For this we need to cooperate with international initiatives such as UNEP FI, which works towards solving global environmental and social issues.

In fulfilling these roles, it would be important to take a precautionary approach. Even where scientific findings include uncertainties, if there is a high risk of a significant negative impact on the environment or society, then it would be beneficial to be attentive and cautious in business. This should be the basic risk response in the 21st century, where future forecasts are increasingly difficult. This risk management function will in turn lead to new business opportunities in financial services.

For its own interest, the financial services sector should also be proactive in the establishment of new markets which add economic value to environmental and social activities.

This set of Principles was drawn up as guidelines for action by financial institutions concerned with the future of the planet and seeking to fulfil their roles and responsibilities in shaping a sustainable society. It is also intended as a starting point for like-minded financial institutions to cooperate without reference to their specific industry types, size and geography. Signatory financial institutions will implement activities based on the “Principles” below, to the extent possible in light of their business context.

The Principles

1. We will recognize our roles and responsibilities, taking into account the precautionary approach, and promote those actions that contribute towards shaping a sustainable society.
2. We will contribute to the formation of a sustainable global society through the development and provision of financial products and services leading to the development and increased competitiveness of “industries contributing to a sustainable society” as represented by the environmental technologies and services sector.
3. From the perspective of regional development and improvement in sustainability performance, we assist the environmental programmes of small and medium enterprises. We will also back activities that will raise environmental awareness amongst citizens and support disaster readiness and community activities.
4. In the formation of a sustainable society we will recognize the importance of cooperation with diverse stakeholders and will not only participate in its activities but will endeavor to take a proactive role.
5. We will not be limited to complying with environmental laws and regulations but will take active steps to reduce our own environmental footprint through resource and energy savings as well as encouraging our suppliers to do likewise.
6. We will recognize activities that will further profile sustainability as a business issue and will endeavor to disclose information on our activities.
7. In order to implement the above actions we will aim to raise the awareness of environmental and societal issues of our own board and support them to take an active role through their normal duties.

Translated by the United Nations Environment Programme Finance Initiative
(UNEP FI)

Asset Management, Securities and Investment Banking Sector Guidelines

1. The role of the asset management, securities and investment banking sectors in achieving a sustainable society

- The asset management, securities and investment banking sectors, as leaders of the financial products market, are expected to be socially responsible for the healthy development of capital markets. As part of this role, it is believed that their appropriate consideration of environmental, social and corporate governance issues (ESG issues henceforth) that may affect corporate values would contribute to the formation of a sustainable society which offers global environmental protection and the growth and development of healthy capital markets.
- As institutional investors, banks, insurers and asset managers, within their asset management operations have an obligation to maximize the long-term benefit of its beneficiaries. For example when making investment decisions, to the extent consistent with their fiduciary responsibilities, considering ESG issues as part of investment decisions and actively engaging with investee companies can raise the awareness of ESG issues and progress initiatives at the investee companies. In addition it is hoped that investors request all companies with investment potential to disclose ESG related information as needed. To achieve these goals, investors together with relevant stakeholders are expected to sophisticate and improve on its techniques in ESG analysis and methods of utilization.
- From the perspective of customer protection, when conducting sales of financial products to investors, securities companies are responsible for providing appropriate information to enable investors to make appropriate investment decisions. As part of this, within the boundaries of laws and regulations, asset managers are expected to contribute to the formation of a sustainable society by providing investors with ESG information of financial products and securities deemed necessary for their investment decision makings. For example in research services, while responding to the needs of investors, security companies are expected to provide necessary ESG information in its analyst reports. Further, based on such research information, asset managers are expected to offer necessary ESG information to its customers at point of sale.
- In its investment banking businesses such as underwriting and structuring of securitized products, investment banks are expected to act as gatekeepers of capital markets in making sure only appropriate financial products are provided. In its agent businesses such as the merger and acquisition advisory services, operations are customer led. In performing these activities, within the boundaries of laws and regulations, investment banks are expected to contribute to the formation of a sustainable society by gathering, analyzing and reflecting ESG information to its businesses operations as necessary and in accordance to its importance to the subject transaction.

2. Practical Actions

In response to the issues mentioned above and in considering practical actions, the following existing standards are referenced as either common to all sectors or unique to the asset management, securities and investment banking sectors.

[Common standards for all sectors]

- ISO 26000 − Guidance on Social Responsibility (November 2010)
- Keidanren (Japan Business Federation) "Charter of Corporate Behavior & Its Implementation Guidance" (Revised September 2010)

[Unique standards for the asset management, securities and investment banking sectors]

- Financial Services Agency "*Guidelines for disclosure of corporate information*"
- Financial Instruments Exchange "Securities Listing Regulations" and "Enforcement Rules for Securities Listing Regulations"
- Financial Instruments Exchange "Preparation Guidelines for the Report on Corporate Governance"
- Expert committee on environment and finance under the Central Environmental Council "Toward Green Finance, a new role for the financial sector in building a low carbon society" (June 2010)
- Principles for Responsible Investment (PRI)
- *Responsible Property Investment (RPI)*
- Japan Securities Dealers Association "Self-regulatory Rules (Articles of Association *and others*)"
- The Investment Trusts Association, Japan "Self-regulatory Rules (Articles of Association *and others*)"
- Japan Securities Investment Advisers Association "Self-Regulatory Rules (Articles of Association *and others*)"
- Japan Securities Dealers Association "*Undertaking Social Contribution Activities within the Securities Industry (Basic Concepts)*" (September 2009)
- Japan Securities Dealers Association "*Securities Industry's Action Plan for Environmental Issues*" (February 2008)
- The Life Insurance Association of Japan "Code of Conduct" (Revised, June 2011)
- The General Insurance Association of Japan "Code of Conduct" (Revised March 2005)

3. Recommended Actions

Signatories in the asset management, securities and investment banking sectors are encouraged to take action proactively in the following areas.

(1) Integrate environmental and social considerations into the operations of its core business (including but not limited to the development of products and services). For example:

<Asset Management Activities>

- Refer ESG-related issues in the standards, regulations and guidelines of asset management and reflect them into the investment and lending decision-making processes.
- Specify ESG considerations in the proxy voting guidelines.
- Accumulate examples of CSR report analysis in the selection of investee companies and utilise them to improve its own CSR activities.
- Utilise comments and advice from external experts to improve its own ESG activities.
- Invest in products which consider ESG issues and contribute to a sustainable society to the extent consistent with its fiduciary responsibilities.
- Proactively encourage investee companies to disclose ESG information and promote awareness and action on ESG issues amongst its suppliers.

<Securities and Investment Banking Activities>

- Explain ESG-related issues to investors via prospectus etc.
- Develop and sell financial products (bonds, mutual funds such as SRI funds, etc.) which offer improvements and/or solutions to ESG-related issues such as environmental issues, micro-finance, social problems (employment issues, childcare, etc.).
- Build donation schemes from the sales of mutual funds such as trust fees that contribute to the improvements and/or solutions to ESG-related issues (same as above).

(2) Integrate environmental and social considerations within its business processes. For example:

- Promote the reduction in paper use by electronic delivery of the prospectus.
- Promote environmental considerations in paper and printed materials such as sales and internal documents.
- Promote paperless meetings and internal documents via the use of information technology.

(3) Disseminate information to society and engage with various stakeholders. For example:

- Externally disclose its asset management and investment activities based on the six principles of the Principles of Responsible Investment.
- Externally disclose on ESG considerations in its proxy voting activities such as its position, structure and voting results.
- Participate in international initiatives related to asset management.
- Appropriately display and/or disclose the purposes and effects of environmental and sustainability related products.
- Promote public awareness on the environment and sustainability issues (such as by holding seminars for students and the business community).
- Promote employee participation in social activities such as environmental protection activities run by communities and other organizations.
- Provide information to investors on its website.

Insurance Sector Guidelines

1. The role of the insurance sector in achieving a sustainable society

- The insurance sector has a distinctive functional role within the financial service sector as it specializes in handling risks. It provides:
  - risk finance by evaluating the economic value of risks and managing and carrying risks,
  - risk solution services such as loss and disaster preventions through use of large amounts of loss and damage data,
  - accumulated information on preventive medicine and health and medical institution networks, etc.
- On the other hand, the emerging issues (so called "environmental, social and governance issues" or "ESG issues") are wide-ranging and complex. For example, we are faced with the issues of climate change mitigation and adaptation, natural resources and energy depletion, food insecurity, poverty and social exclusion, an aging population, localized depopulation, structural issues in health care, pension schemes and elderly nursing care, health issues, safety and disaster prevention, human rights, and so forth. In solving these problems, it is possible to utilise the functions and roles of the insurance sector featured above. For example, internationally, the role of insurance in climate change adaptation and micro-insurance is drawing attention. Also, in Japan, the insurance sector is increasingly complementing the social security system in areas such as medical care, pensions and nursing care.
- The insurance sector will function more effectively in fulfilling its role in achieving a sustainable society by collaborating with investment, lending and other financial institutions coordinating with policy and partnering with various sectors such as international organisations and civil society.
- Through these initiatives, the insurance sector is expected to mitigate long-term risks and thereby contribute to the development of a globally inclusive society with sustainable, safe, secure and vigorous local communities.

2. Practical Actions

In response to the issues mentioned above and in considering practical actions, the following existing standards are referenced as either common to all sectors or unique to the insurance sector.

[Common standards for all sectors]

- ISO 26000 － Guidance on Social Responsibility (November 2010)
- Keidanren (Japan Business Federation) "Charter of Corporate Behavior & Its Implementation Guidance" (Revised September 2010)

[Unique standards for the insurance sector]

- UNEP Finance Initiative "Principles for Sustainable Insurance" (Forthcoming June 2012)
- The Life Insurance Association of Japan "Code of Conduct" (Revised June 2011)
- The Life Insurance Association of Japan "Action Guidelines for Environmental Issues" (November 2006)
- The Life Insurance Association of Japan "Life Insurance Industry's Commitment to a Low Carbon Society" (February 2011)
- The General Insurance Association of Japan "Code of Conduct" (Revised March 2005)
- The General Insurance Association of Japan "The Environment Policy of The General Insurance Association of Japan" (Revised June 2006)
- General Insurance Industry "Action Plan for the Preservation of the Environment" (March 2006)
- Action Policy and Plan of the Environmental Sub-committee of The General Insurance Association of Japan

3. References to Good Practice Examples

- UNEP Finance Initiative, Principles for Sustainable Insurance "The Principles in Action --- Case studies from around the world" (Forthcoming June 2012)
- Input to the UNFCCC from the United Nations Environment Programme and the United Nations Environment Programme Finance Initiative (February 2011)
- A Ceres Report From Risk to Opportunity 2008: Insurer Response to Climate Change (September 2009)
- Results of the survey on the current state of CSR activities of financial institutions conducted by the Financial Services Agency (February 2006)
- Websites of the General Insurance Association of Japan and the Life Insurance Association of Japan and CSR reports etc. of insurance companies offers case studies and examples

4. Recommended Actions

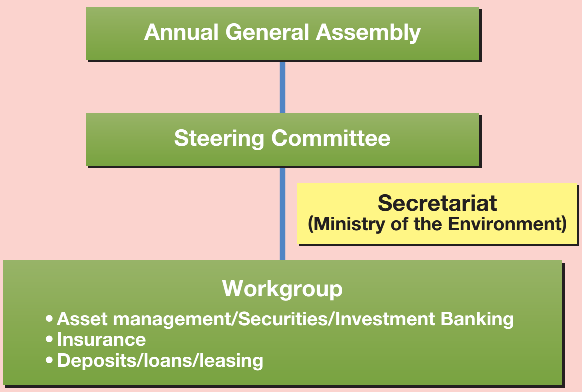
Signatories in the insurance sector are encouraged to take action proactively in the following areas:

(1) Integrate environmental and social considerations into the development of financial products and services. For example:
- Endeavor to widely disseminate and propose policy measures to accelerate the development of insurance products and services that mitigate risks associated with the development of green technology and environmental business opportunities.
- Assess the relevancy and connections between ESG issues and insurance underwriting and rate calculation processes.
- Integrate ESG issues into risk solution services such as risk and vulnerability assessment, loss prevention, loss control service, and business continuity management.

(2) Integrate environmental and social considerations into business processes. For example:
- Promote the sustainable use of materials, especially paper documentations used throughout the overall value chain such as application forms, charters, insurance policies or manuals used to offer explanations to customers.
- Draft and execute a carbon emission reduction plan for transportation, logistics and office-based activities and operations.

(3) Disseminate information to society and engage with various stakeholders. For example:
- Disclose activities through corporate social responsibility reports and other channels.
- Join international initiatives on insurance particularly those that address ESG issues.
- Promote social action programmes among employees, such as reforestation, local nature protection and biodiversity conservation projects.
- Promote the development of personnel in the field of disaster prevention. Raise awareness of the availability of natural disaster insurance such as earthquake insurance through school and consumer education programmes.
- In the non-life insurance sector, promote ecological and safe driving behavior.
- In the non-life insurance sector, promote use of recycled materials.
- Promote and support the development of personnel in the field of health and nursing care. Raise awareness of the availability of medical and nursing care insurance through medical institutions, and school and consumer education programmes.
- Promote preventive health and check-ups by supporting and offering information to academic and medical institutions and offering school and consumer education programmes.

Governing Structure of the Principles



Deposits, Loans and Leasing Sector Guidelines

1. The role of the deposits, loans and leasing sectors in achieving a sustainable society

- Financial institutions engaged in the deposits, loans and leasing sectors are expected to contribute to solving environmental and social issues through their businesses. Their roles are diverse and depend on its business contents and the characteristics of its customers. By considering the sustainability of society when undertaking its financial intermediary functions (i.e. information production and risk-underwriting functions), each signatory institution is expected to provide positive impacts to both the providers and recipients of capital.
- Support towards the transition to a sustainable society is a challenge that may be pursued within the conduct of the deposits, loans and leasing businesses. They include activities such as undertaking environmental measures, developing finance mechanisms for new funding demands in the fields investing in sustainable society, and the utilising of leasing functions to promote eco-products.

2. Practical Actions

In response to the issues mentioned above and in considering practical actions, the following existing standards are referenced as either common to all sectors or unique to the deposits, loans and leasing sectors.

[Common standards for all sectors]

- ISO 26000 − Guidance on Social Responsibility (November 2010)
- Keidanren (Japan Business Federation) “Charter of Corporate Behavior & Its Implementation Guidance” (Revised September 2010)

[Unique standards for the deposits, loans and leasing sectors]

- The Japanese Bankers Association “Code of Conduct” (November 2005)
- The Japanese Bankers Association “Banking Industry Action Plan for the Environment” (September 2001)
- The National Association of Shinkin Banks “Shinkin Banking Industry Action Plan for the Environment” (July 2007)
- The National Association of Shinkin Banks “Policy on Environmental Activities of Shinkin Banks” (November 2010)
- National Central Society of Credit Cooperatives “Credit Cooperatives Action Plan for the Environment” (October 2007)

3. Recommended Actions

Signatories in the deposits, loans and leasing sectors are encouraged to take action proactively in the following areas.

(1) Integrate environmental and social considerations into the development of financial products and services in its core business. For example:

- Support corporate borrowers in integrating environmental and social considerations in its management techniques and equipment purchases and assist activities that strengthen the competiveness of related businesses.
- Endeavor to be updated on how increasing environmental risks affect the business of its customers.
- For loans to large-scale development projects, assess its social and environmental impacts. Where impacts are significant, necessary measures should be taken such as to call for action against the borrowers.
- In collaboration with various stakeholders, endeavor to secure the flow of funds in the region.
- Provide financial mechanisms to meet new funding demands in the construction of a sustainable society such as the maintenance of environmental infrastructures.
- Develop and promote financial products that finance a sustainable society such as eco deposits.
- Within the leasing business, contribute to a sustainable society by taking advantages of the financial and equipment procurement functions of leasing. For example, promote equipment and facilities with high environmental performances, supporting energy and resource conservation efforts, take reduce-reuse-recycle (3R) approaches and make appropriate disposal of leased property.

(2) Integrate environmental and social considerations within its business processes. For example:

- Consider green procurement of paper and other resources used across the value chain (application forms, agreements, securities, manuals, etc.) and work on its resource efficiency and recycling.
- Develop and implement plans to reduce carbon emissions from premises, company-owned cars, movement of people and logistics.
- Consider environmental performances of capital investment (procurement of premises, equipment, etc.) such as the use of recycled resources.

(3) Disseminate information to society and engage with various stakeholders. For example:

- Appropriately display and/or disclose the purposes and effects of environmental related products.
- With the cooperation of customers, reduce own environmental impacts through energy efficiency of premises, digitalizing of forms, etc.
- Promote environmental awareness raising activities at schools, amongst consumers, etc.
- Promote employee participation in social activities such as local nature and biodiversity conservation activities.
- Endeavour to contribute to the development of environmental industries by exchanging environmental information between companies.
- Endeavour to raise the environmental awareness of its customers by providing national and international information on environmental issues.

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Developing Principles for Financial Action towards a Sustainable Society

Background

In June 2010, the “Expert Committee on Environment and Finance” under the Central Environmental Council (chaired by Mr. Takejiro Sueyoshi (Special Advisor to UNEP Finance Initiative)) issued a report titled “Towards Green Finance, the New Role of the Financial Sector in Building a Low Carbon Society”. This report included a policy recommendation for establishing the “Principles for Financial Action towards a Sustainable Society” aiming at expanding environmentally friendly finance in Japan.

With the passionate chairperson, Japanese financial institutions from most of the financial sub-sectors (such as financial holding companies, banks, trust banks, cooperative financial institutions, securities firms, insurance companies, and asset management companies) voluntarily participated in the Drafting Committee. The Ministry of the Environment Government of Japan supported the process as the Secretariat.

The plenary Drafting Committee meetings were held seven times in total from September 2010 through October 2011, consisting of extensive discussions. For the sake of establishing Sector Specific Guidelines and discussing how each sector should take action in line with the core Principles, the following working groups were created: Deposit/Loan/Leasing, Asset Management/Securities/Investment Banking, Insurance and General/Follow-up. Meanwhile, the Great East Japan Earthquake in March 2011 changed people’s minds and attitudes to reconsider global “Sustainability” beyond the “Environment”.

Structure of the Principles

(1) “Foreword” and “Preamble”
“Foreword” outlines a statement which may be modified to better convey the roles financial institutions should play in any unanticipated era to come, by referring only to issues with higher materiality to reflect our changing circumstances. On the other hand, “Preamble” declares the universal and fundamental nature of the relevancy between the roles of the sustainable society and financial business.

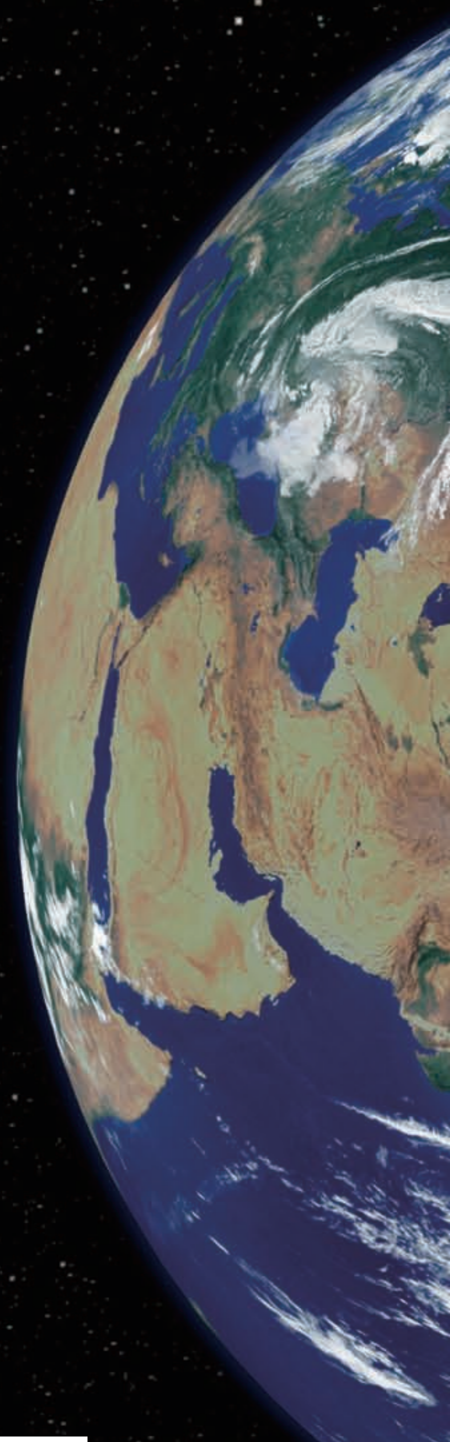
(2) The Principles and Guidelines
The “Principles” comprise generic contents and have been accepted by signatories; while the “Guidelines” show concretely to some extent how to implement the Principles for sub-sectors as a guide.

The Principles in Relation to Global Initiatives Such as UNEP FI and PRI

The philosophy and direction of the Principles are consistent with those of global initiatives such as UNEP FI and PRI.

Financial institutions in Japan must be relevant in the discussions of sustainability on a global scale. The roles and responsibilities assumed by the financial institutions in each region, as well as their contribution to the Japanese economy and regional economy, will be the key to help tackling global issues.

Hence, one of the missions of the Principles is to function as a stepping stone to initiatives in order to incorporate sustainable finance into regional society.



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Written and edited by Secretariat of the Drafting Committee for Environmental Finance Principles, Ministry of the Environment Government of Japan

First Edition: March 2012

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