GAIL Asia Pacific

Impact Lawyers Journal

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Impact Law in the Region

An Overview of Sustainability and Climate Reporting in Singapore

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Japan's Impact Practices + Legal Issues

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IMPACT LAW IN JAPAN

Welcome to the 2024 Q4 edition of the GAIL Asia Pacific Impact Lawyers Journal

In this issue, we continue to focus on the topics that occupy impact lawyers - this time on developments in Japan.

Our lead articles are from **Takahisa Watanabe** and **Sotaro Hotta**, both GAIL APAC Regional Board members and impact lawyers. In "Japan's Impact Practices Advancing through Public-Private Partnerships", Takahisa reviews the recent trends in and present status of impact practices in Japan, particularly in terms of the Japanese government's approach to impact investment, impact start-ups, and the social sector. He highlights how Japan's impact practices have been rapidly gaining recognition, and its framework is being developed in a unique collaboration between the government and the private sector. In "Legal Issues in the Use of Blended Finance in Japan', Sotaro and Takahisa draw attention to the legal issues in blended finance, particularly in the context of its use in impact finance in Japan. They conclude that to widen the use of blended finance, it will be necessary to accumulate and share practical knowledge of realistic structures; and increase the number of concessional fund providers from the private sector, local authorities, and public financial institutions.

Our reports on Impact law in the region continue with updates and overviews on Singapore from Elsa Chen & Alyssa Tjioe and Joesph Chun, and on China from Giana Lin.

This Journal is a place where impact lawyers can share their experience and expertise, with a particular focus on issues of interest in the Asia Pacific region.

We welcome contributions from any source. Please send your suggestions, comments and contributions to The Editor, GAIL Asia Pacific Impact Lawyers Journal at journal@gailnet.org.

ABOUT GAIL ASIA PACIFIC

The Global Alliance of Impact Lawyers (GA!L) is a global community of legal leaders using their careers to have a positive impact on people and the planet.

The goal of GAIL is to bring lawyers together into a community where we can share knowledge and best practices, support our common efforts, and work for change – all in service of the vision of a sustainable and responsible world economy.

GAIL is organised into various geographic regions so that its activities and programmes can be tailored to local interests and timezones.

Currently there are Regional Boards for Africa, Asia Pacific, Europe, Latin America, North America, and the UK.

Membership of a region is open to any impact lawyer, legal academic or law student who resides in that region. In the case of the Asia Pacific Region, the timezones covered stretch east/west from Pakistan to the Pacific Islands and north/south from China to Australia/New Zealand.

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For membership information see page 36 and the membership page on GAIL's website www.gailnet.org/join

IN THIS ISSUE

A MESSAGE FROM THE
APAC REGIONAL CHAIR

Dr. AMMARA FAROOQ MALIK
Chair of APAC Regional Board for GAIL

Welcome to the 4th edition of the GAIL Asia Pacific Impact Lawyers Journal. This issue focuses on the dynamic developments in Japan's impact law landscape.

Our lead articles feature insights from Takahisa Watanabe and Sotaro Hotta, GAIL APAC Regional Board members. Takahisa's article, 'Japan's Impact Practices Advancing through Public–Private Partnerships,' explores the evolving impact practices in Japan, emphasizing the government's collaborative approach with the private sector. Sotaro and Takahisa's joint piece, 'Legal Issues in the Use of Blended Finance in Japan,' addresses the legal complexities of blended finance in impact investments, advocating for increased practical knowledge and participation from various sectors.

Additionally, we provide updates on impact law from Singapore and China, contributed by Elsa Chen, Alyssa Tjioe, Joseph Chun, and Giana Lin. We also highlight recent GAIL APAC events leading up to the final event of the year on "Bridging Investment Readiness with Impact: Knowledge Exchange between Asia and Europe"

This journal serves as a platform for impact lawyers to exchange expertise and insights, particularly within the Asia Pacific region. Many thanks to the Editorial Committee, particularly Joseph Chun, for his brilliant suggestions and the editing of this edition.

We hope you find this edition enriching and enlightening! ■

Ammara

Impact Law in the Region

01

AN OVERVIEW OF SUSTAINABILITY AND CLIMATE REPORTING IN SINGAPORE

and

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Sustainability and climate reporting regulations in Singapore are currently developing at a rapid pace as Singapore aims to drive consistency, credibility and comparability across climate-related disclosures. This reflects the shift from the view of sustainability reporting as a means of stakeholder engagement to a means of monitoring the impacts of climate change and sustainability issues on business activities, and vice versa.

In June 2016, the Singapore Exchange ("SGX") elevated sustainability reporting requirements for listed issuers from a voluntary basis to a "comply or explain" basis through amendments to the Singapore Exchange Securities Trading Limited ("SGX-ST") Listing Rules (Mainboard) and the SGX-ST Listing Rules (Catalist) (together, the "Listing Rules"). In September 2024, the Singapore Exchange Regulation ("SGX RegCo") further amended the Listing Rules for all issuers to adopt the International Sustainability Standards Board ("ISSB") Standards for climate-related disclosures on a mandatory basis, moving towards consistency and comparability of climate-related disclosures across capital markets globally from 1 January 2025.

This article aims to provide an overview of the sustainability and climate reporting requirements in Singapore.

THE MOVE TOWARDS MANDATORY SUSTAINABILITY AND CLIMATE DISCLOSURES FOR ISSUERS IN SINGAPORE

Since 2011, issuers in Singapore have used environmental, social, and governance ("ESG") metrics as part of their framework for sustainability reporting.[1] In 2020, SGX further recommended a list of 27 Core ESG metrics for sustainability reporting. This would include metrics such as water consumption, employment statistics, occupational health and safety, and certifications received by the company. Climate-related disclosures specifically refer to disclosures on how an entity's activities affect, and are affected by, climate change. While environmental metrics and climate-related metrics are linked, as a topic, climate change is increasingly unbundled from ESG topics as a standalone reporting pillar with additional financial-related metrics due to the critical nature of climate change risks, and the need to urgently incorporate climate considerations into financial and business decisions to meet global environmental objectives.[2]

As governments deepen and accelerate efforts to mitigate and adapt to climate change, the tracking of efforts and progress in emissions reduction in a transparent and meaningful manner to allocate capital towards the most impactful sustainable projects is now more critical than ever. Climate accounting and disclosures are taking centre stage key to provide consistent, comparable and verifiable data towards such ends. SGX has signalled that the reliability and verifiability of climate and ESG information is an area that SGX is keeping a close eye on,[3] including making statements that climate information is becoming as material as financial information, and that the same kind of enforcement action could be seen being taken for material gaps and misstatements in climate disclosures.

1 - https://api2.sgx.com/sites/default/files/2021-12/Response%20Paper%20on%20Starting%20with%20a%20Common%20Set%20of%20Core%20ESG%20Metrics.pdf
2 - https://api2.sgx.com/sites/default/files/2021-08/Consultation%20Paper%20on%20Climate%20and%20Diversity%20-%20The%20Way%20Forward.pdf
3 - https://www.sgxgroup.com/media-centre/20220719-keynote-speech-tan-boon-gin-ceo-sgx-regco-climate-reporting-asean

The Sustainability Reporting Advisory Committee ("SRAC"), set up by the Accounting and Corporate Regulatory Authority ("ACRA") and SGX RegCo in June 2022, in developing a sustainability reporting roadmap for Singapore-incorporated companies, also considered that companies which are able to demonstrate that they are ahead in their decarbonisation journeys gain access to new markets, customers, and financing, whereas companies slow to react risk losing out to competitors and face exclusion from value chains for not adequately addressing climate risks.

This is in recognition of the growing relevance of sustainability reporting[4] in influencing investment allocation decisions by investors, separate from government efforts, as it facilitates risk awareness associated with environment or society aspects and is a way for a company to demonstrate that it is actively managing non-financial risks, positioning itself to capture opportunities from global shifts and investing for the long-term. Use of globally consistent, credible, and comparable sustainability-related metrics also helps to facilitate comparison between companies for investment purposes, which in turn helps businesses remain competitive.

It is also timely that sustainability reporting is picking up steam in Singapore as companies incorporated in Singapore would nonetheless be affected by sustainability reporting requirements in other jurisdictions with extraterritorial reporting scopes, such as the European Union ("EU"). Singapore's national framework on sustainability reporting thus also aims to keep pace with sustainability reporting requirements and compliance practices required by international counterparties and ensure sustainability reporting frameworks are contextualised to local requirements. Hence, as international sustainability disclosure standards and frameworks continue to evolve, ACRA and SGX have stated that they will issue guidance on the interoperability, use of, and transitional reliefs for the various standards and frameworks.

KEY REGULATIONS IN SINGAPORE IN RELATION TO SUSTAINABILITY AND CLIMATE REPORTING

- **For issuers listed on the Singapore Exchange:** Per Listing Rules 711A and 711B, SGX-listed issuers are required to prepare an annual sustainability report containing the following primary components on a "comply or explain" basis: (i) material environmental, social and governance factors, (ii) climate-related disclosures consistent with the Task Force on Climate-related Financial Disclosures ("TCFD") recommendations; (iii) setting out sustainability policies, practices, performance and targets in relation to material ESG factors; (iv) sustainability reporting framework; and (v) a board statement.

Per Listing Rule 710A, issuers are also required to set a board diversity policy that addresses gender, skill and experience, as well as other relevant aspects of diversity. Issuers must describe the board diversity policy and details relating to the diversity targets, plans, timelines and progress in their annual reports.

4 - https://www.pmo.gov.sg/Newsroom/DPM-Heng-Swee-Keat-at-the-Launch-of-the-SGX-Sustainability-Reporting-Review

Aside from mandatory disclosures, as set out above, SGX further recommends a list of 27 Core ESG Metrics for issuers to use as a starting point for sustainability reporting. They include metrics such as greenhouse gas ("GHG") emissions, occupational health and safety, age-based diversity, and alignment with frameworks.

- **For retail funds:**

Per Circular No. CFC 02/2022 issued by the Monetary Authority of Singapore ("**MAS**"), companies offering retail funds that include or use ESG-related or similar terms in its name and are lodged with MAS on or after 1 January 2023 must comply with specific disclosure and reporting guidelines. Such funds should also reflect an ESG focus in its investment portfolio and/or strategy.

Circular No. CFC 02/2022 also sets out MAS' expectations on how existing requirements under the Code on Collective Investment Schemes ("CIS Code") and the Securities and Futures (Offers of Investments) (Collective Investment Schemes) Regulations 2005 ("SF(CIS)R") apply to retail ESG funds.

- **For financial institutions ("FI"s):**

Per MAS' Guidelines on Environmental Risk Management ("**EnRM Guidelines**"), financial institutions ("FIs") are expected to make regular and meaningful disclosure of their environmental risks, including with reference to international reporting frameworks, such as the TCFD framework, so as to enhance market discipline by investors.
FIs are to implement the Guidelines in a manner commensurate with the size and nature of its activities as well as its risk profile. While the EnRM Guidelines are not legally binding and intended to promote certain best practices to be taken into consideration by FIs, how well an institution observes the guidelines and assesses, monitors, mitigates and discloses its risk exposures will factor into MAS' overall risk assessment of banks and insurers.

KEY INTERNATIONAL SUSTAINABILITY STANDARDS AND FRAMEWORKS USED IN SINGAPORE

Currently, Singapore's mandatory sustainability reporting requirements are focused on financial materiality of climate-related disclosures. This reflects Singapore's commitment to transition towards a low-carbon and climate-resilient economy.[5] SGX plans to review during later public consultations a few years down the road, or when new thematic sustainability standards are released, whether mandatory adoption of the ISSB Standards will be required for the reporting of financially material sustainability-related information beyond climate-related disclosures. However, keeping in mind that investors continue to value sustainability reporting for insights into the quality of management and future prospects of the company, and that sustainability reporting contributes to enterprise value through communication with external and internal stakeholders on other risk factors, disclosures of sustainability-related information beyond climate-related disclosures are required. This is reflected in the current "comply or explain" approach to the reporting of the primary components of the sustainability report including material ESG factors, which will soon be mandatory.

5 - https://www.nccs.gov.sg/media/press-release/submission-of-singapores-enhanced-nationally-determined-contribution-and-long-term-low-emissions-development-strategy/

> **THE ISSB STANDARDS ARE SIGNIFICANT BECAUSE IT BUILDS ON AND HARMONISES THE WORK OF MARKET-LED INVESTOR-FOCUSED REPORTING INITIATIVES.**

Sustainability standards and frameworks facilitate the flow of comparable and consistent sustainability and climate-related information across jurisdictions. They are complementary and designed to be interoperable. Where they differ is that sustainability standards provide specific, detailed and replicable disclosure requirements for various sustainability topics, including metrics to be used, whereas sustainability frameworks provide principles-based guidance on how information is structured, how it is prepared, and which broad topics to cover.

In Singapore, the most commonly used sustainability reporting framework is the Global Reporting Initiative ("**GRI**") Standards. For climate-related disclosures, the most used climate-related disclosures framework is the TCFD framework, which was mandatory for listed issuers on a phased approach up till the amendments to the Listing Rules in 2024 for the ISSB Standards to replace the TCFD framework for mandatory climate-related disclosures by listed issuers in Singapore. The ISSB Standards fully incorporates the TCFD framework and can be seen as the culmination of the work of the TCFD. Hence, issuers already using the TCFD framework are generally in a good position to comply with the ISSB Standards.

- **ISSB Standards:**
The purpose of the ISSB is to develop standards that provide a global baseline and common language to ensure that investors globally have access to material sustainability information that has strong linkage with financial statements.[6] This reflects financial materiality in the context of sustainability reporting, whereby a sustainability topic is significant if it may trigger financial impacts for businesses, such as by affecting the ability of an undertaking to continue to use, or obtain, resources.

The ISSB Standards are significant because it builds on and harmonises the work of market-led investor-focused reporting initiatives, namely the Climate Disclosure Standards Board ("**CDSB**"), the Value Reporting Foundation's Integrated Reporting Framework and industry-based Sustainability Accounting Standards Board ("**SASB**") Standards, as well as the World Economic Forum's Stakeholder Capitalism Metrics, in addition to the TCFD framework. More than 20 jurisdictions representing more than 55 per cent of global GDP have begun the process of introducing the ISSB Standards in their legal or regulatory frameworks.[7]

The IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information ("**IFRS S1**") and IFRS S2 Climate-related Disclosures ("**IFRS S2**") are the first two sustainability disclosure standards published by the ISSB. IFRS S1 sets out the basic requirements for a complete set of sustainability-related financial disclosures to meet the needs of global capital markets, and IFRS S2 is a topic-based standard which sets out requirements for disclosing information about an entity's climate-related risks and opportunities. They are meant to be used together, but adopting jurisdictions may choose how to transpose the

6 - https://www.ifrs.org/groups/international-sustainability-standards-board/
7 - https://www.ifrs.org/news-and-events/news/2024/05/jurisdictions-representing-over-half-the-global-economy-by-gdp-take-steps-towards-issb-standards/

ISSB Standards into their regulatory framework.

In Singapore, from the financial year commencing on or after 1 January 2025, the mandatory baseline requirement for climate-related disclosures will be to disclose information on climate-related risks and opportunities that apply all the requirements in IFRS S2, aside from the disclosure of Scope 3 emissions, and to then consequently apply the provisions in IFRS S1 that apply to climate-related disclosures.

The ISSB is currently also developing industry-based metrics, with the intention of making them mandatory in the future. There are also currently two reporting standards in development, on the topics of biodiversity, ecosystems and ecosystem services and human capital.

- **GRI Standards:**

The purpose of the GRI Standards is to provide a global baseline and common language to ensure that a multi-stakeholder audience has access to information on the economic, environmental, and social impacts of an entity's business activities. This is considered impact materiality in the context of sustainability reporting, whereby a sustainability topic is significant if it may have actual or potential impacts on people or the environment, such as whether the business of the company contributes to pollutive outcomes, or results in significant improvements to the welfare of a local community.

The GRI Standards are the most widely used global framework for sustainability reporting, and in Singapore, 99 per cent of issuers on the SGX currently use the GRI reporting framework.[8] SGX continues to recommend the use of the GRI Standards to report on the primary components such as sustainability policies, practices, performance and targets in the updated Practice Note 7.6. SGX has also released an illustrative sustainability report in collaboration with the Institute of Singapore Chartered Accountants to demonstrate how companies can use the ISSB Standards with the GRI reporting framework. Hence, it is expected that companies will continue to use the GRI reporting

8 - https://bschool.nus.edu.sg/cgs/wp-content/uploads/sites/7/2023/11/CGS-SGX-Sustainability-Reporting-Review-2023_Report.pdf

framework alongside the ISSB Standards on a voluntary basis to meet the requirement to communicate sustainability information.

Other sustainability reporting frameworks: The SASB Standards will be used as the foundation for the industry-based metrics which will be mandatory in future, and are useful in identifying financially material topics for industries.

- The ISSB Standards also require companies to consider the SASB Standards in the absence of specific IFRS Sustainability Disclosure Standards, and the ISSB will continue to maintain and enhance the SASB Standards.

The Integrated Reporting Framework provides principles-based guidance for reporting structure and content, and the IASB and ISSB are jointly responsible for the Integrated Reporting Framework. It is focused on the concepts of value creation, preservation or erosion in the financial, manufactured, intellectual, human, social and relationship, and natural capitals over time.[9] In Singapore, 2 per cent of issuers have adopted the Integrated Reporting Framework.[10]

FUTURE DEVELOPMENTS

ACRA and SGX have agreed on the following timeline:[11]

1. Listed issuers are to report climate-related disclosures on Scope 1 and 2 GHG emissions by the financial year beginning on or after 1 January 2025, and Scope 3 GHG emissions for the larger issuers tentatively by the financial year beginning on or after 1 January 2026. These climate-related disclosures must be prepared in accordance with the requirements on climate-related disclosures set out in Practice Note 7.6, which is consistent with the ISSB Standards;[12]

2. Listed issuers are to report on the primary components of a sustainability report beyond climate-related disclosures on a mandatory basis from the financial year beginning on or after 1 January 2026;[13]

3. Large non-listed companies with annual revenue more than or equal to S$1 billion and total assets more than or equal to S$500 million are to report on ISSB Standards-aligned climate-related disclosures on Scope 1 and 2 GHG emissions by the financial year beginning on or after 1 January 2027.

4. External limited assurance for Scope 1 and 2 GHG emissions should be obtained by listed issuers from the financial year beginning on or after 1 January 2027, and large non-listed companies from the financial year beginning on or after 1 January 2029.

In addition, further public consultations will be conducted on legal responsibilities and sanctions in due course.[14] ■

9 - https://integratedreporting.ifrs.org/wp-content/uploads/2024/05/IFRS-IR-GettingStarted-051524.pdf
10 - https://bschool.nus.edu.sg/cgs/wp-content/uploads/sites/7/2023/11/CGS-SGX-Sustainability-Reporting-Review-2023_Report.pdf
11 - https://www.sgxgroup.com/media-centre/20240228-climate-reporting-help-companies-ride-green-transition
12 - https://www.sgxgroup.com/media-centre/20240923-sgx-regco-start-incorporating-ifrs-sustainability-disclosure
13 - https://api2.sgx.com/sites/default/files/2024-09/Response%20Paper%20-%20SR%20-%20Enhancing%20Consistency%20and%20Comparability%20%28final%29_0.pdf
14 - https://www.acra.gov.sg/docs/default-source/default-document-library/legislation/listing-of-consultation-papers/climate-reporting-and-assurance-roadmap/response-to-public-consultation-on-climate-reporting-and-assurance-roadmap-for-singapore.pdf

SINGAPORE: THE USE OF TRANSITION CREDITS TO FINANCE CLIMATE TRANSITIONS

Impact Law in the Region

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Singapore state-owned investment firm Temasek's investment platform GenZero, infrastructure company Keppel and ACEN, the energy unit of Philippine conglomerate Ayala Corporation, entered into a memorandum of understanding (MoU) in August 2024 to study the development of a first-of-its-kind transition credit project in the Philippines to accelerate the retirement of a South Luzon coal-fired power plant (CFPP) in Batangas city in 2030 – 10 years ahead of schedule – and its replacement with a solar plant and a battery storage system.
The acceleration of retirement will require extra financing to bring forward the building of a replacement renewable energy system combining wind and solar farms with battery storage, and switching to the new energy system will bring up the cost of electricity compared to coal.

The project to leverage carbon credits to enable the early decommissioning of a CFPP and replacement with renewable energy while ensuring a just transition, is a world-first. It is led by the Coal to Clean Credit Initiative (CCCI), an initiative of The Rockefeller Foundation and the Global

Energy Alliance for People and Planet, and is a collaboration with ACEN and supported by the Monetary Authority of Singapore (MAS). CCCI is developing a methodology to calculate the emissions reduction credits that could be issued, and the methodology is currently under review by Verra, the manager of the Verified Carbon Standard Programme. There are also other project (individual)-based and sectoral (jurisdictional)-based transition credit methodologies in development, but none has been finalised. Important criteria to ensure the credits meet the Integrity Council of Voluntary Carbon Markets' Core Carbon Principles and Article 6 integrity requirements include additionality and permanence, so loss-making plants will not be eligible for credits, and developers must ensure that the plant is permanently shut down and also prevent leakage through a commitment to not build new coal plants, and by ensuring the emissions impact of additional power to replace the plant is included in emissions reduction calculations. The avoidance of leakage may require government commitment as reflected in their national energy policy. Another important criteria is the existence of a just transition plan with clearly identified stakeholders, impact and mitigation measures.

Although China and India dominate coal-fired generation, Southeast Asia is home to the fourth-largest number of CFPPs globally, and its network is also among the youngest, with an average age of less than 15 years. CFPPs are costly to build, and their owners expect to recover their investment over a period of 40 to 50 years. To attract private capital for credible early and managed phase-out of CFPPs, the *Singapore-Asia Taxonomy for Sustainable Finance* launched by the MAS in December 2023 has set out facility-level, entity-level and power-system-level criteria for eligibility for classification as transition finance under the taxonomy. The idea behind the creation of transition credits is to close the financing gap for the costs of the phase-out that private and concessional capital cannot cover, such as lost revenues to plant owners, the premium associated with investing in replacement assets, such as battery storage, and the just transition costs.

MAS also launched the Transition Credits Coalition (TRACTION) in December 2023. It comprises more than 30 members and knowledge partners, including financial institutions and investment managers, insurance advisors, exchanges and traders, carbon service providers, NGOs, industry organisations, and international organization, the Asian Development Bank, and the Rockfeller Foundation. TRACTION, inter alia, supports the generation of high-integrity transition credits, enables transition credits transaction scalability, and bolsters buyers' confidence and trust in transition credits, and the retirement of the plant in Batangas city is one of two pilot projects to test the feasibility of integrating transition credits for early plant retirement, and pave the way for other plants and countries in the region to follow suit. This initiative complements other ongoing initiatives.

While the current focus of transition credits is on financing early CFPP retirement, they could at a later stage also potentially be used to finance the transition of other carbon-intensive sectors.

The MoU follows the signing of another MoU between Singapore and the Philippines the same month to work towards a legally binding implementation agreement for cross-border carbon credit transfers in alignment with Article 6.2 of the Paris Agreement. The Singapore government had earlier announced its readiness to offtake transition credits if they meet Singapore's standards for environmental integrity. ■

THE IMPACT OF THE 2024 UPDATES TO CHINA'S COMPANY LAW ON CORPORATE SOCIAL RESPONSIBILITY (CSR)

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The newly revised Company Law of the People's Republic of China came into effect on July 1, 2024. This revision introduced several substantive changes, including detailed provisions related to Corporate Social Responsibility (CSR). These regulations are not only reflected in the legal text but are also noteworthy in their practical application, which readers should consider.

I OVERVIEW OF CSR PROVISIONS IN THE REVISED COMPANY LAW

Among the key changes in the 2024 updates to the Company Law, Article 20 stands out as central to Corporate Social Responsibility (CSR). It mandates that companies consider the interests of stakeholders (such as employees and consumers) and broader public interests (like environmental protection) in their business activities. Additionally, companies are encouraged to engage in public welfare initiatives and disclose CSR reports.

Two other significant provisions also contribute to the CSR framework:

Article 19 emphasizes the need for companies to comply with laws and uphold ethical business practices, while remaining accountable to both government and public supervision. Article 180 specifies the duties of loyalty and diligence for directors, supervisors, and senior management. They must avoid conflicts of interest, act in the best interest of the company, and manage company affairs with care. These responsibilities extend to controlling shareholders or actual controllers, even if they do not hold formal positions within the company.

a The Legal Significance of the Revised Company Law

At first glance, these provisions may seem non-mandatory. So, why are they important? Four key points highlight the significance of the revised Company Law in relation to CSR.

b Providing a Legal Basis for CSR Reporting by All Companies

For authorities to impose mandatory obligations, they need a higher-level legal foundation. Without legal requirements, companies may lack the motivation to disclose CSR activities. Article 20 now extends CSR reporting obligations to all companies, not just listed companies. While not mandatory, this law provides a firmer basis for CSR compliance than moral obligations alone, establishing for the first time a legal foundation for companies to consider stakeholders beyond just shareholders.

c The "Three Interests" Framework: Private, Stakeholder, and Public Interests

Article 20 introduces the concept of balancing three types of interests: private interests (shareholders and investors), stakeholders (employees, suppliers, consumers, and even competitors), and public interests (environmental protection, renewable energy use, and pollution prevention).

A traditional challenge is whether investments in public interests might conflict with private interests, potentially leading to breaches of fiduciary duty. When a company focuses on maximizing shareholder value, allocating resources to stakeholders or public interests could be seen as a violation of this duty. Article 180 clarifies this issue by defining to whom the fiduciary duty is owed.

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Article 180 outlines several fiduciary duties, including the duty of loyalty, which requires a focus on the company's overall best interests, not just those of the shareholders.

II RESPONDING TO THE CHANGES AND THEIR IMPACT ON CSR

a Prepare for CSR Reporting Requirements

While full enforcement may not occur immediately, based on current trends, companies that fail to issue CSR reports could stand out negatively as policy and market drivers evolve.

b Plan CSR Efforts Holistically

Some companies, due to industry regulations or government directives, may already be preparing CSR reports. At the outset, it is crucial to select appropriate standards (establishing an effective evaluation system) and develop a comprehensive CSR strategy.

c Align Internal CSR Policies and Systems

CSR should not be confined to a single department; it must be integrated across all relevant departments. Systems should be established to ensure continuous and effective communication between departments.

d Clarify the Authority of the Board of Directors

In light of the corporate governance framework discussed earlier, the powers and responsibilities of the board and its directors must be clearly outlined. Additionally, governance measures should address risk management, internal controls, audits, and compliance processes.

In summary, the revised Company Law provides clear guidance and strong support for CSR implementation. Moving forward, companies can adopt a proactive approach by focusing on these four areas, turning legal CSR requirements into tangible business actions. ■

ARTICLE 19 EMPHASIZES THE NEED FOR COMPANIES TO COMPLY WITH LAWS AND UPHOLD ETHICAL BUSINESS PRACTICES

ARTICLE 20 STANDS OUT AS CENTRAL TO CORPORATE SOCIAL RESPONSIBILITY (CSR)

02 RECENT GAIL APAC EVENTS

12 NOVEMBER

Bridging Investment Readiness with Impact: Knowledge Exchange between Asia and Europe

The in-person panel discussion explored various aspects of impact investment, including the evolving focus on impact investment readiness, and impact-driven strategies going beyond ESG risks. Through market trends and case studies from Asia and Europe, it also focussed on the importance of generating positive outcomes in investment decisions and facilitating agenda alignment between investors and companies. The event was moderated by GAIL Europe Board Member Raluca Radu, and speakers included fellow Board Member Gabriel de Almeida and GAIL APAC Board Member Viven Teu.

31 OCTOBER

Connecting the Global South to the Global North: Accelerating Impact Law Knowledge Sharing

Focussing on how legal frameworks can support sustainable development, climate action, and social justice across diverse jurisdictions, this webinar aimed to bridge the gap between legal professionals from different regions and foster collaboration and the sharing of best practices in impact law. It was moderated by GAIL APAC Member Amal Farooq Malik; and GAIL APAC Chair Ammara Farooq Malik was a speaker.

12 SEPTEMBER

Practical Impact of EU CSRD/CSDDD on Asian Companies

This webinar brought together ESG experts from Europe and Asia to explore the implications of the EU's Corporate Sustainability Reporting Directive (CSRD) and Corporate Sustainability Due Diligence Directive (CSDDD) on Asian companies. It was moderated by GAIL APAC Board Member, Takahisa Watanabe, and speakers included fellow Board Member, Viven Teu, and GAIL Europe Chair, Emiliano Giovine.

20 AUGUST

Blended Finance – APAC Legal Perspectives

Experts from various fields, including GAIL APAC Board Members, Vivien Teu, Sotaro Hotta, and Michael Ryland, shared insights on the legal, financial, and practical aspects of utilising blended finance in emerging markets to advance sustainable development goals (SDGs) in this hybrid seminar, focusing on its challenges, regulatory hurdles, and the importance of collaboration for scaling its impact.

9 MAY

APAC Impact Law Initiatives – From Climate Contracts to Blended Finance

This in-person roundtable was organised in collaboration with LITE Lab@HKU x TCLP Climate Contracting Initiative to discuss GAIL APAC's recently published "Unlocking the Legal Pathways for Blended Finance" report, in particular its Asian case studies, as well as recent initiatives to develop green legal documentation in Singapore, Hong Kong and beyond. Speakers at the event included GAIL APAC Board members, Brian Tang and Vivien Teu.

22-23 APRIL

GAIL Annual Summit 2024

This two-day GAIL Annual Summit held in London created opportunities for structured networking and expert knowledge sharing on key topics across impact disciplines and the most recent market developments, including impact investing, blended finance, climate change and the law, corporate governance, purposeful business, innovative legal structures, supply chains, philanthropic ventures, and ESG regulatory frameworks.

The GAIL APAC Regional Board took part in various sessions, highlighting areas of impact specific to the region. See the 'Insight' section of the website for recordings of these.

Impact In Japan

03

JAPAN'S IMPACT PRACTICES ADVANCING THROUGH PUBLIC–PRIVATE PARTNERSHIPS

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Since 2022, impact practices in Japan have been expanding at an accelerating pace. In particular, Japan's impact practices are unique in that the public and private sectors are working together to build a foundation for impact practices. This paper looks at trends in impact practices in Japan over the past few years and then introduces the status of impact practices in Japan in terms of the Japanese government's approach to impact investment, trends surrounding impact start-ups, and trends in the social sector.

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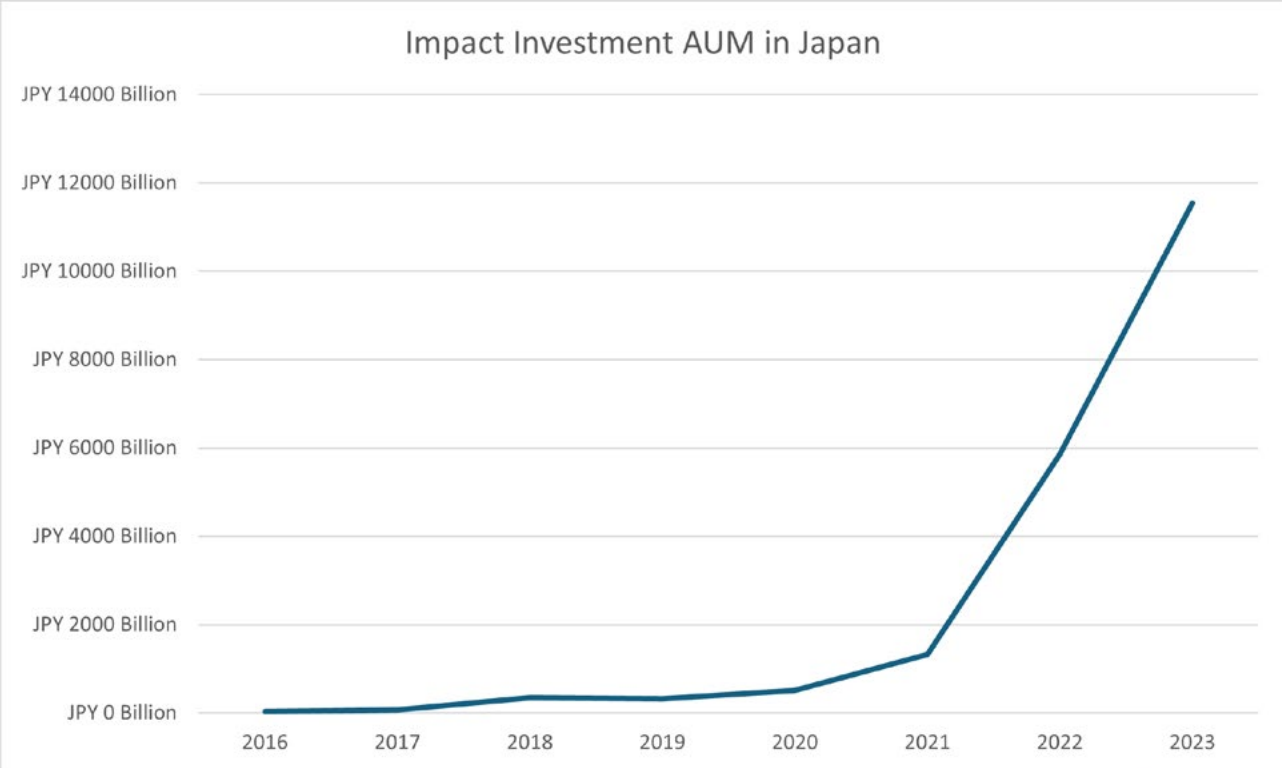
Trends in Impact Practices in Japan

M/Y	Sector	Details
June 2019	Public	Prime Minister Abe declares at the G20 Osaka Summit that Japan will take the lead in innovative financing schemes, such as impact investing and dormant bank accounts
June 2020	Public	Study session on impact investing co-hosted by the Financial Services Agency (FSA) and the Global Steering Group Japan National Advisory Board (now GSG Impact JAPAN National Partner)
July 2020	Public	Ministry of the Environment releases "Concept Paper on Impact Finance"
November 2021	Private	Inauguration of the Japan Impact-driven Financing Initiative
June 2022	Public	The government's new basic policy clearly states the promotion of impact investment
June 2022	Private	Keidanren (Japan Business Federation) releases "Using Impact Metrics to Promote Dialogue with Purpose as Starting Point"
September 2022	Public	"The Study Group on Impact Investment for Global Health" launched by the Cabinet Secretariat
September 2022	Public	Tokyo Metropolitan Government establishes the Social Impact Investment Fund
October 2022	Public	FSA establishes "Working Group on Impact Investment"
October 2022	Private	Impact Startup Association launched
January 2023	Private	Keizai Doyukai (Japan Association of Corporate Executives) member volunteers establish a fund management company "&Capital" to promote impact investment in Africa
May 2023	Public	Cabinet Secretariat announces "Impact Investment Initiative for Global Health" at the G7 Hiroshima Summit
June 2023	Public	FSA publishes "Report by the Working Group on Impact Investment" and "Basic Guidelines for Impact Investing (Draft)"
July 2023	Private	Keizai Doyukai enters into the "Partnership Agreement for Collaboration" with the Impact Startup Association and the Japan Association of New Public.
October 2023	Public	The Ministry of Economy, Trade and Industry (METI) launches J-Startup Impact, a program to foster and support impact start-ups through collaboration between the public and private sectors

M/Y	Sector	Details
October 2023	Public	Prime Minister Kishida's speech at Principles for Responsible Investment (PRI) notes the importance of impact investing in Japan
November 2023	Public	FSA holds inaugural meeting for the establishment of the Impact Consortium, a public–private partnership council on impact investing
March 2024	Private	B Market Builder Japan (BMBJ) established as an official partner of B Lab, which is responsible for promoting B Corp certification in Japan
March 2024	Public	FSA publishes "Basic Guidelines on Impact Investment (Impact Finance)"
May 2024	Private	The Impact IPO Working Group of GSG Impact JAPAN releases "Guidance for Impact Companies on Disclosure and Dialogue in Capital Markets - Version 1"
June 2024	Public	The Cabinet and the Cabinet Secretariat clearly state the promotion of impact investment and support measures for impact start-ups in the "Grand Design and Action Plan for a New Capitalism 2024 Revised Version," which also specifies that the Cabinet will consider taking initiatives based on the arrangement where impact investment by the Government Pension Investment Fund (GPIF) does not fall under consideration of other matters

Particularly after 2022, various public–private partnerships have been launched one after another, and interest in impact investment has been growing. As shown in the table below, the assets under management (AUM) of impact investment is also increasing at an accelerating pace. In fact, a survey of 58 domestic impact investment organizations conducted by GSG Impact Japan in its "Current State and Challenges 2023 of Impact Investing in Japan"[15] reported that the majority (55%) of responding organizations commenced impact investment in 2020 or later. The report also indicates that while non-listed equities (58%) accounted for the largest number of asset classes for impact investment based on the number of responding organizations, loans (43%) and listed equities (23%) accounted for 66% of the total investments in terms of investment balance. This is also significant in light of the fact that private equity accounted for 26% of the AUM base in the GIIN survey,[16] making it the largest. In other words, private equity, which is still relatively small in size, accounts for the majority of impact investments in Japan.

15 - https://impactinvestment.jp/user/media/resources-pdf/gsg-2023_en.pdf
16 - Global Impact Investing Network (GIIN). 2023 GIINsight: Impact Investing Allocations, Activity & Performance - https://thegiin.org/publication/research/2023-giinsight-series/



Source: Prepared by the author based on a report by GSG Impact JAPAN.

Japanese Government's Approach to Impact Investment

Beginning with Prime Minister Abe's announcement at the G20 Osaka Summit in June 2019, the Japanese government has been actively promoting impact investment through collaboration among relevant ministries and agencies, including the Ministry of the Environment, the FSA, and the Cabinet Office. However, there is no government-led legislative regulation in Japan. Given the lack of accumulated information on impact investment, the government is working to deepen discussions by communicating and collaborating with the private sector to formulate and promote an understanding of impact investment.

Establishment of Basic Guidelines on Impact Investment

First, the Positive Impact Finance Task Force was established by the Ministry of the Environment in March 2020, and it released the "Concept Paper on Impact Finance" in July 2020 and the "Starting from the Green: A Guide to Impact Assessment" in March 2021. These documents present the basic elements of impact finance and a guide for impact evaluation in a manner consistent with international trends in impact finance, with the aim of promoting the practice of impact finance in Japan.

Subsequently, in October 2022, the FSA established the Working Group on Impact Investing, and in March 2024, published the Basic Guidelines on Impact Investing (Impact Financing) (the "Guidelines")".

The Guidelines were published after significant revisions were made based on public comments.

While the draft of the Guidelines initially referred to “principles” for impact investment, in light of the lack of sufficient investment practices in Japan, the term “principles” was revised to “elements.” Therefore, unlike the so-called soft law guidelines of public authorities, the Guidelines do not indicate the conditions that need to be fulfilled in order for an investment to qualify as an impact investment. The Guidelines also differ in nature from regulations such as the EU’s Sustainable Finance Disclosure Regulation (SFDR); the Guidelines clearly state that they are not necessarily expected to be used by third-party organizations to evaluate the applicability of impact investing.

There were also changes in the elements of impact investment. In the original draft of the Guidelines, impact investment was based on the premise of securing a certain return on investment (i.e. including concessional financing but excluding donations), and it identified:

1. intentionality;
2. additionality;
3. identification/ measurement/ management;
4. innovation/ transformation/ acceleration (support for novelty) as the primary principles of impact investment.

However, (1) and (2) were modified, and support for novelty was removed (details are shown in the table below). Finally, the basic elements of impact investment were defined as:

1. intention;
2. contribution;
3. identification/ measurement/ management;
4. innovation/ transformation/ acceleration.

Comparison of Elements/Definition of Impact Investment	
Concept Paper on Impact Finance	1. Intended to have a positive impact at least in one aspect, on the assumption that a material negative impact is appropriately mitigated/ managed in all environmental, social, and economic aspects. 2. Conduct impact assessment and monitor elements 3. Disclose information on the results of impact assessment and element monitoring 4. Seek to ensure an appropriate risk-return profile for individual financial institutions/investors from a medium- to long-term perspective
Draft Basic Guidelines on Impact Investment	Principle 1 (intentionality): intended "social or environmental impact" **and "profitability"** is clarified **Principle 2 (additionality): additional impact is expected through the investment** Principle 3 (Identification, measurement, and management of impact): Identifying, measuring, and managing impact Principle 4 (innovation/transformation/acceleration): Support **novelty that could lead to accelerate** transformations in markets and customers
Basic Guidelines on Impact Investment (Final)	Element 1 (intention): intended "social or environmental impact" is clarified Element 2 (contribution): investment contributes to realizing impact Element 3 (Identification, measurement, and management): Identifying, measuring, and managing impact Element 4 (innovation/transformation/acceleration): Support transforming or accelerating transformations in markets and customers
GIIN*	Investments made into companies, organisations, and funds with the intention to generate social and environmental impact alongside financial returns. ■ Intentionality ■ Investment with return expectations ■ Range of return expectations and asset classes ■ Impact measurement

* - https://thegiin.org/publication/post/about-impact-investing/#what-is-impact-investing

Global Alliance of Impact Lawyers

Additionality has been pointed out as being difficult to assess, particularly for listed investments, and there is no explicit reference to additionality in the U.S. GIIN definition. That omission is consistent with the fact that the Guidelines cover investments in a wide range of asset classes. In addition, it is assumed that the “support for novelty” element in the Draft Guidelines was also mentioned as a special characteristic of Japan, as the study group responsible for formulating them had been discussing impact investment with a particular focus on investment in start-ups, but the Final Guidelines were ultimately revised based on public comments.

The Guidelines are not limited in terms of the types of investments, investment entities, and asset classes covered, but rather include a wide range of investments, including listed and private equity investments, debt and real assets, and investments by asset owners and foundations. Therefore, these modifications of the elements of impact investing are consistent with this approach.

While the definition of “impact investing” in Japan remains under discussion and the Guidelines are not binding, they are expected to be highly influential in shaping Japan’s impact finance market in the future.

Based on these Guidelines, further discussions are expected to be held in the Impact Consortium described in the following section.

Launch of Impact Consortium

From the viewpoint of providing opportunities for investors and companies to further engage in mutual discussions, in November 2011, the “Impact Consortium” was established as a forum for public–private partnership dialogue to promote impact investment and financing, and the following four subcommittees were established:

Working Group	Summary
Working Group on Data and Indicators	■ Holds discussions on the focus and collection methods of data and indicators, such as how to set indicators for impact investment and how to collect and estimate data at the time of investment implementation, with reference to leading examples from Japan and abroad. ■ Holds discussions on the **development and operation of a database that contains data and indicators specific to Japan and connects to international databases.**
Working Group on Market Research and Formation	■ **Organizes overviews of the impact investment market in Japan and discusses challenges and solutions to expanding the market.** ■ **In the first year, the focus will be on public markets**, where the basic concepts of impact investment practice have not yet been established, to organize issues in investment and disseminate the essentials of impact investing in listed markets for practitioners.
Working Group on Local Finances and Evaluation Practices	■ Carries out discussions and initiatives that arouse interest and make it easy to understand the potential for local value creation and other initiatives that incorporate perspectives on solving a wide range of social and environmental issues. ■ **By facilitating various means of communication, supporting momentum building and networking, and strengthening the flow of human and financial resources to local areas, the aim is to realize a virtuous cycle in which solutions to environmental and social issues and growth are mutually complementary and are reinforced through various innovations originating in local areas.**
Working Group on Promotion of Public–Private Partnerships	■ Particularly discusses the **promotion of solutions to social issues through collaboration between government and impact start-ups.** ■ Provides structured presentations on issues that exist on the government side and the impact start-up side, and discusses the direction and methods of problem solving. ■ The goal is to create products that consolidate information on impact start-up solutions, know-how, and case studies that contribute to public–private partnerships, and to study ways to disseminate and promote their use, leading to the creation of future case studies.

Developments related to the GPIF

The GPIF, a signatory to the PRI and a leading advocate for ESG investment in Japan, has adopted the stance of engaging in ESG investments but not in impact investments at this time, as such investments do not align with its investment approach, which prohibits using pension funds for the purpose of realizing specific objectives or measures (consideration of other matters). On the other hand, the GPIF has emphasized the importance of impact measurement, indicating that its direction is consistent with the philosophy of impact investing.

Under these circumstances, it is noteworthy that in the "Grand Design of New Capitalism and Implementation Plan 2024 Revised Version," approved by the Cabinet on June 21, 2024, the government has expressed its view that the GPIF's consideration of non-financial factors, including impact and ESG, does not constitute "other considerations", and that the GPIF will consider taking initiatives based on such understanding. The GPIF's stance on impact investing may change in the future as a result of these policy decisions; if the GPIF enters the impact investing market, it is expected to further expand the impact investing market, similar to what has happened with ESG investing.

Trends in Impact Start-ups

As mentioned above, impact start-ups, which are companies that aim to solve social and environmental issues and realize sustainable economic growth, are attracting attention in Japan in relation to impact investment, and the government has included them in its policies.[17]

In the private sector, the Impact Startup Association was established in 2022. The association, which currently has 138 start-ups as members, aims to support the growth of impact start-ups and to promote the creation of an ecosystem for impact start-ups.[18] In July 2023, the association concluded the Partnership Agreement for Collaboration between the Keizai Doyukai and the Japan Association of New Public and it is working to solve various social issues through collaboration between large corporations and start-ups, effectively utilizing their respective resources and working together.

In addition, in October 2023, METI established "J-Startup Impact," a public-private partnership impact start-up support program, and selected 30 companies that are expected to serve as role models. The selected companies will receive support for exhibiting at large-scale events in Japan and abroad, overseas local support, expansion of bidding opportunities, and matching with private companies, in addition to promoted use of expert consultation services for measuring and managing impacts and acquiring global certifications, and support in communicating and PR at various events in Japan and abroad.[19]

17 - The "Grand Design and Implementation Plan for a New Capitalism, Revised 2024" also clearly states the promotion of impact investment and support measures for impact start-ups.
18 - https://prtimes.jp/main/html/rd/p/000000015.000109519.html
19 - https://www.meti.go.jp/press/2023/10/20231006008/20231006008.html

Trends in Social Sector

In the social sector, private corporations are expected to be proactively involved in services that have been provided by the government, and the government has indicated that it is considering introducing "a new form of corporation in which the private sector plays a public role (Japanese version of a public benefit corporation)."

Also, in Japan, the "Act on Utilization of Funds Related to Dormant Deposits to Promote Public Interest Activities by the Private Sector" came into effect in 2018, and the Japan Network for Public Interest Activities (JANPIA) has been providing grants to promote private sector public interest activities by utilizing dormant deposits to address various social issues (support for children and youth, support for those who have difficulty making a living, and support for regional revitalization).

Starting in 2024, JANPIA will engage in equity investments to promote private sector solutions to social issues. JANPIA positions itself as an impact-first investor (wholesaler) and is expected to play a major role as a concessional capital provider in Japan.

In addition, on March 1, 2024, BMBJ was established as an official partner of B Lab, an organization that promotes B Corp certification. B Corp certification is an international certification granted to companies that conduct business activities in a socially and environmentally friendly manner, and the number of companies acquiring this certification is increasing in Japan. BMBJ aims to contribute to the B Corp movement in Japan by providing support to companies seeking certification, disseminating information, and building a community. These efforts are expected to lead to the spread of a new business model in which companies not only fulfill their social responsibilities but also use them as a competitive advantage.

Conclusion

Japan's impact practices have been rapidly gaining recognition, especially in the last two years, and its framework is being developed in a unique Japanese movement of collaboration between the government and the private sector. Such efforts in Japan are based on the premise that impact investing is not just a passing trend, but an important economic activity for achieving a sustainable society, and it will be interesting to see how impact practices in Japan evolve and what kind of social impact they will have. ■

Impact In Japan

LEGAL ISSUES IN THE USE OF BLENDED FINANCE IN JAPAN

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Introduction

Blended finance is attracting global attention, and its use is spreading steadily, especially as the forum for international financial cooperation and is positioned as a key instrument for mobilizing finance to achieve SDGs. In response to this trend, GAIL published a report entitled "Unlocking Legal Pathways for Blended Finance Case Studies and Global Insights" on April 20, 2024, in which more than 40 lawyers in 13 jurisdictions with expertise in advising on blended finance structuring mapped blended finance regulations and case studies.

Blended finance has drawn increasing attention in Japan as well, with the promotion of "social finance" under the government's "New Form of Capitalism" and the growing attention to and interest in impact investment, for example, the guidelines for impact investment[20] published by the Financial Services Agency in March 2024 contain references to blended finance.

This article reviews and summarizes the legal issues in blended finance, with a focus on its use in impact finance in Japan.[21]

Overview of Blended Finance

1 What is Blended Finance?

Blended finance does not refer to a specific financial instrument or market, but is a financing method that focuses on the purpose and source of funding. Although there is no unified definition of blended finance, and the definition varies slightly depending on the organization and purpose, to date, blended finance has been used in two main contexts.

The first is development finance. An enormous investment is required to achieve the Sustainable Development Goals by 2030; thus, it is necessary to mobilize both private and public funds[22]. Attention has been focused on blended finance to mobilize additional financing for sustainable development in developing countries. In this context, the blended finance efforts are led by multinational development banks (MDBs) and development finance institutions (DFIs). In Japan, there are also several examples of such blended finance, with the Japan International Cooperation Agency (JICA) playing a central role. Blended finance is also attracting attention in the context of transition finance, and the Net-Zero Asset Owner Alliance (NZAOA), an international initiative of asset owners (including insurance companies and pension funds), is committed to transitioning its investment portfolio to net zero by 2050. Japanese participants of NZAOA include Dai-ichi Life Insurance, Nippon Life Insurance Company, Sumitomo Life Insurance, Meiji Yasuda Life Insurance Company, and SOMPO Holdings, Inc.

The second context is impact finance. Unlike development finance, impact finance involves distinctive investments in domestic and overseas social enterprises and projects. As a contributor to concessional capital, it is assumed that a broader range of players, such as foundations and charities, will participate in this type of funding. For example, it has been noted that concessional finance has played an important role in impact investing, in terms of risk supplementation for general investors interested in impact investing and other factors[23], and concessional capital

20 - Financial Services Agency, "Basic Guidelines on Impact Investment (Impact Finance)" (March 2024) at page 9 (https://www.fsa.go.jp/singi/impact/siryou/20240329/02.pdf)
21 - It is necessary to pay attention to various regulations, depending on the attributes of the investors in the blended finance and geographical factors, especially with regard to projects involving overseas development financing.
22 - United Nations Conference on Trade and Development, "World Investment Report 2023-Investing in Sustainable Energy for All," (July 5, 2023) at page 30.
23 - Financial Services Agency, "Basic Guidelines on Impact Investment (Impact Finance)" (March 2024) at page 4 footnote 5.

contributions have attracted investment from a broader range of investors.

In recent years, in Japan, there have been growing expectations that the private sector will utilize concessional capital-type blended finance in the context of contributions to impact investment, from perspectives such as lowering financing costs.[24] One example of this is the discussion of blended finance in the context of impact finance in the aforementioned FSA's guidelines for impact investment.

2 How to design a blended finance structure?

Blended finance is a mechanism that increases the amount of available funds by allowing investors to participate in seeking commercial returns through concessions by investors interested in public returns. This is why the structure is designed in terms of relatively risk-tolerant concessional funds covering the first loss portion. The method of funding, including concessional funds, covers debt instruments such as social impact bonds (SIBs)[25]; equity, such as stock, is the primary option, but grants and more concessional funding from charitable organizations, subsidies from governmental agencies, and tax incentives also play key roles[26]. Blended finance is designed by combining these methods, or by creating a tiered structure, with different returns, using only a single method.
In Japan, there are no regulations or mechanisms specific to blended finance, but it is possible to create such structures by combining existing instruments such as partnership agreements, preferred shares, senior/mezzanine debts.

As an example, consider the Japan ASEAN Women Empowerment Fund, in which both JICA and the Japan Bank for International Cooperation (JBIC) invested in Luxembourg corporate funds, and equity was prioritized in senior, mezzanine, and first-loss shares. Market-rate commercial investors participated in the highest-priority senior shares, and public financial institutions (JICA and JBIC) invested in the second-tier mezzanine shares. BlueOrchard, which organizes and manages the fund, invests in the most subordinate tier of the fund, which bears first losses.[27]

Debt funds are designed as concessional funds through the use of unsecured or low value collateral, as well as lower interest rates, and by adjusting principal and interest payment dates (e.g., by establishing grace periods or grace conditions after the loan is made).

In the case of equity funds, in addition to common shares, there may be differences in the amount and terms of dividends and the existence of redemption rights, through the use of class shares (preferred and subordinated shares).

When designing these products, it may be possible to combine the concept of revenue share/profit share, in which repayments or dividends are deferred until a certain amount of revenue

24 - Financial Services Agency, "Basic Guidelines on Impact Investment (Impact Finance)" (March 2024) at page 9.
25 - For example, in Japan, the Toyonaka Giving Up Smoking Project utilized SIBs to provide funds of a different nature: loans from financial institutions, investments from foundations, and investments from individuals within the framework of public-private partnerships.
26 - See also: Tej Dhami & Mark O'Donnell, "UK Catalytic Capital: Growing Provision, Catalysing Impact " (May 2023) for a description of the common features, advantages, and disadvantages of these measures.
27 - Convergence, "Japan ASEAN Women Empowerment Fund Case Study" (March 2020) at page 3.
28 - There are two methods for the capped dividend structure: an annual dividend cap, and establishment of a cap on the returns earned by the investors, both of which are used overseas.

is generated, and capped dividends, through which a certain upper limit on dividends is set to support sustainable business growth.[28] When using social impact bonds, it also is possible to incorporate an impact-linked concept, such as a reduction in interest rates when a specific impact target (outcome trigger) is achieved.

3 Blended Finance Vehicles

There are several options for the legal vehicles used to consolidate funds and promote projects when implementing blended finance, and various approaches are used in different countries, depending on the applicable legal system[29]. Since there are no laws in Japan that establish or regulate the vehicles themselves, it is assumed that the vehicle will be created in the form of a fund (investment limited partnership) or corporate entity, such as a joint stock company, and funds such as subsidy or grant of profit-making enterprises, charitable organizations, investment funds, development finance, and government funds are consolidated therein[30].

Legal Considerations in Blended Finance

1 Investment agreement issues

When using blended finance, particular attention should be paid to various factors including the different interests of the investors and the increased complexity of contractual relationships arising from the blended finance structure as described above. For example, even if an entity is established in the form of a joint stock company and finances are aggregated, it is assumed

29 - See: Global Alliance of Impact Lawyers, "Unlocking Legal Pathways for Blended Finance: Case Studies and Global Insights," (20 April 2024) at page 24, for more information on vehicles available for blended financing in different countries.
30 - As blended finance has the same financial documents as concessional funds and for-profit funds, it has been pointed out that tax and accounting procedures may become more complicated in different countries.

that individual investment and loan agreements and shareholder agreements will be necessary in addition to project agreements. The differences in interests may affect the governance structure, and it is assumed that certain investors will bear more risk and may or may not have differing interests in the degree of involvement in governance, such as the right to elect directors, and in reporting requirements, such as ensuring consistency with missions and reporting of impact KPI, as well as in the methods of determining the use of funds, and these issues need to be reflected in relevant agreements. This needs to be sorted out in the early stages of structuring and term sheet discussions, with experts being commissioned on a case-by-case basis.

2 Issues when forming funds

Two cases are envisaged in which blended finance is used by a fund: (i) when blended finance is used to raise funds at the fund level, and (ii) when blended finance is used at the level of investment execution by the fund. As the issues relating to option (ii) are the same as those relating to investment agreements, this section focuses on the case of option (i). In addition, when setting up a fund in Japan, the most promising option is an investment limited partnership under the Limited Partnership Act for Investment, so this article focuses on investment limited partnerships as fund vehicles.

To clarify, the hypothetical use of blended finance in the fund in this article assumes that investors who become limited partners will receive dividends of profits or distributions of assets relating to the invested business in excess of the amount of their contributions. Accordingly, a separate examination is required for a donated blended finance that does not enjoy any return from the fund.

a. Issues under the Financial Instruments and Exchange Act

In principle, interests in partnership-type funds are deemed securities under the Financial Instruments and Exchange Act (FIEA), so (again, in principle) the fund operator is required to register as a Type II financial instruments business operator to solicit the acquisition of interests in the funds on its own and as an investment management business operator to manage the money invested in the fund directly. However, if the investors in the fund include one or more qualified institutional investors and 49 or fewer investors subject to 'specially permitted services' and meet other statutory requirements, the fund operator can solicit interests in the fund and manage the fund by just filing a notification. In the event of registration or notification under the FIEA, the fund operator must comply with various regulations set forth in the FIEA, including a prohibition on compensation for loss, the principle of suitability, and the regulations on reciprocal transactions between proprietary trading and assets under management.

b. Fund agreement issues

As an initial matter, it is necessary to determine whether it is possible for investors who pursue market-level returns and investors who are risk-conscious, such as those who contribute concessional funds, to join the same fund as limited partners with junior and senior relationships. Since the "cash value of one unit of contributions must be uniform" (Limited Partnership Act for Investment, Article

6, Paragraph 3), it can be widely construed that the equity interests in an investment limited partnership must be uniform. However, according to the wording of the same paragraph, it is straightforward to consider that the paragraph specifies only a uniform amount of one-unit investments, and that it is not necessary that the content of the shares be uniform[31]. In addition, given the published opinion that the purpose of this provision is to require uniformity of amounts for purposes of convenient equity calculations[32], it is considered legally possible to establish the content of partnership interests according to the risk orientation of each investor. However, if there is a transfer of economic profits from certain investors to others, there may be situations in which tax considerations are necessary, for example, to determine whether the transfer may be deemed a gift or donation. Having said that, after the appropriate tax analysis, a tiered hierarchy of junior and senior limited partners could be set up. It is expected that the arranged waterfall structure will be adopted with regard to distribution provisions. Similarly, liquidation provisions need to be established in line with the distribution terms, and provisions relating to ownership interests in fund assets and shares of profits and losses need to be adjusted in accordance with the junior-senior structure of the fund.

Drawing on the global

31 - Nishimura Asahi Law Office, “The Finance Law Grand [Complete Revision] (Part 1)” (August 2017) at page 357.
32 - Ministry of Economy, Trade and Industry “ Explanation of Separate Articles for Limited Partnership Act for Investment” (revised June 1, 2005) at page 45.

discussion, we can say that, in Japan, it also is possible to differentiate between the rights of each limited partner, not only in terms of financial return, but also in terms of involvement in governance of the fund, including the investment committee and advisory committee, and reporting transparency, for example, by establishing favorable terms for investors in concessional funds who are taking higher risks. Consideration also can be given to clauses requiring refunds of investments in concessionary funds if the fund's investment activity deviates from the original purpose defined in the agreement, or linking the remuneration of the general partner with the fund's achievement of impact KPIs.

Toward Wider Use of Blended Finance

In this article, we have offered an overview of blended finance mechanisms and relevant legal issues in Japan.

However, blended finance is not actively used in Japan at the present time, and obstacles to its use have been pointed out, including the complexity of the blended finance structure, the need to customize it on a project-by-project basis, and the need to coordinate the interests of various stakeholders[33]. In this respect, it will be necessary to accumulate and share practical knowledge of realistic structures, for example, by using structures that are appropriate to the size of the transaction.

In addition, Japan has few concessional fund providers, which play an important role in the implementation of blended finance. To expand the use of blended finance, it is crucial to increase the number of players that can contribute concessional funds from the private sector, such as charities, angel investors, and family trusts, as well as local authorities and public financial institutions.

In the UK, Better Society Capital, a wholesaler of impact investments that utilizes dormant assets, has a strong presence in the blended finance sphere; wholesaler impact funds like Better Society Capital are expected to be important catalysts for projects, as concessional fund providers. Better Society Capital is also actively involved in efforts to promote blended finance, for example, by disseminating information on blended finance. In Japan, the Japan Network for Public Interest Activities (JANPIA), an organization that utilizes dormant assets to promote public interest activities by the private sector, may from 2024 do so through equity investments, in addition to grants which they had previously been permitted to do. Given their role in managing dormant assets with a public character, JANPIA is expected to play a significant role in the future by catalyzing purely private money as a source of the concessional capital, which is a major issue in blended finance. ■

33 - See comments (https://thegiin.org/blended-finance-working-group/) in Global Impact Investing Network (GIIN).

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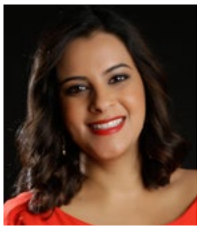

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