

Latest Trends in Climate Change Regulations and Policies in Japan

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1. Introduction

In recent years climate change has become an increasingly important topic of discussion in countries and regions all around the world; so much so that many jurisdictions around the globe have established, or attempted to establish regulations that are intended to reduce environmental damage. Given this situation, stakeholders are paying a lot of attention to the policies and regulations that are being implemented in each jurisdiction and how these trends are affecting the global economy. Specifically, in Japan, various policies and regulations have been developed in recent years, with the aim of combating climate change, and as it is important for foreign and domestic investors to understand them, this paper is intended to provide foreign investors insight into Japan's policies and regulations in this area.¹

2. Comprehensive Climate Change Policies and Regulations

Firstly, we will touch on Japan's comprehensive policies and regulations that aim to combat climate change.

The primary comprehensive policies and regulations that are of primary concern to foreign investors include the following: (i) the GX Promotion Act; (ii) the Act on Promotion of Global Warming Countermeasures; (iii) the Climate Change Adaptation Act; (iv) the Green Growth Strategy; and (v) the Grand Design and Action Plan for a New Form of Capitalism, 2023 Revised Version. This paper will briefly explain each of these policies and regulations below.

(1) GX Promotion Act

On June 30, 2023, the GX Promotion Act came into force, as an effort to realize a decarbonized society by 2050. In order to achieve this purpose, Japan will need GX investments from both the public and private sectors, in excess of 150 trillion yen over the next ten years, while simultaneously strengthening its industrial competitiveness and increasing its economic growth rate. This Act was formulated pursuant to the "Basic Policy for the GX Realization," the purpose of which is to enhance the industrial competitiveness of the Japanese economy and economic growth by creating new demand and markets in the fields of stable energy supply and

¹ Attorney Yuko Hashimoto was the primary author of Section 2 of this newsletter, and attorney Keita Yasui was the primary author of Section 3.

decarbonization through acceleration of GX.

The aspects of the GX Promotion Act which are of particular importance to foreign investors are as follows:

(i) Issuance of GX Economy Transition Bonds

To support upfront investment in the promotion of GX, the Japanese government decided to issue public bonds called GX Economy Transition Bonds for ten years, starting in 2023. The policy, entitled, “Basic Policy for the GX Realization” states that support in the amount of 20 trillion yen will be provided for the transition to non-fossil forms of energy, such as renewable energy and nuclear power, transformation of the industrial structure on both the supply and demand sides in various industries, especially manufacturing industries, such as steel and chemical manufacturing, promotion of drastic energy conservation measures, and investments in research and development of various fields, such as resource circulation and carbon fixation technology, among other efforts. The plan is to redeem the GX Economy Transition Bonds by 2050, using fossil fuel surcharges and contributions from specified business operators, as described below.

GX Economy Transition Bonds are different from green bonds, pursuant to which use of the funds is limited to environmental improvement efforts, such as global warming countermeasures and renewable energy, and they are believed to be the world’s first national transition bonds; the permitted uses of the funds include projects that contribute to the transition to decarbonization.²

(ii) Introduction of Growth-Oriented Carbon Pricing

This is a system by which to “price” carbon emissions, and the plan is to introduce the system with low charges initially, and increase the charges gradually. It was decided that fossil fuel surcharges will be collected from fossil fuel importers and other, similar business operators starting in fiscal 2028. These surcharges depend on the amount of CO₂ originating from imported fossil fuels and other similar fossil fuels, and that starting in fiscal 2033, CO₂ emission allowances will be allocated (by amount) to power generating business operators (some of which will be charged). Furthermore, contributions from specified business operators will be collected depending on the aforementioned allocated amounts. The plan is to determine the specific allocations and unit prices to be charged for emissions allowances via an auction.

(iii) Establishment of GX Promotion Organization

Per the approval of the Japanese Minister of Economy, Trade and Industry, it has been decided to establish an Organization on Promotion of a Transition to a Decarbonized Growth-Oriented Economic Structure (GX Promotion Organization). The GX Promotion Organization will focus on operations, such as support for GX investments made by private-sector companies, collection of fossil fuel surcharges, contributions from specified business operators, and management of the emissions trading system. Support for GX investments made by private-sector companies includes loan guarantees by the GX Promotion Organization. Guarantees from the GX Promotion Organization should make it easier for financial institutions to finance businesses and companies subject to the transition, and for those businesses and companies to procure funds.

² https://www.meti.go.jp/english/policy/energy_environment/transition_finance/index.html

(2) Act on Promotion of Global Warming Countermeasures

On July 1, 2022, an act entitled, “Act Partially Amending the Act on Promotion of Global Warming Countermeasures” came into force, and amended the Act on Promotion of Global Warming Countermeasures³ (“Global Warming Countermeasures Act”), which was enacted in 1998. The Global Warming Countermeasures Act is a law that establishes the framework pursuant to which the national government, local governments, business operators, and citizens make joint efforts to combat global warming, following the adoption of the Kyoto Protocol at the third session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP3). This amendment represents the eighth amendment to the Act.

The details of the Global Warming Countermeasures Act are as follows:

(i) Reporting the Amount of GHG Emissions

The Global Warming Countermeasures Act obligates specified business operators to report their greenhouse gas (GHG) emissions amount to the national government. The subjects of the reporting obligations are categorized as “energy-derived CO₂” and “GHG other than energy-derived CO₂.” The specific business emitters A⁴ and specified carrier emitters⁵ must report on “energy-derived CO₂”, and specific business emitters B⁶ must report on “GHG other than energy-derived CO₂.” If a business operator fails to report the amount of emissions or makes a false report, a penalty, consisting of an administrative fine of up to 200,000 yen, will be imposed. However, it is worth noting that the Act only imposes reporting obligations, and does not create obligations for business operators to reduce emissions.

The data compiled by the government was digitized by an amendment in fiscal 2021, and is open to the public, rendering disclosure request procedures unnecessary and making it possible for anyone to access the information.

(ii) Establishment of New Basic Principles Based on the Paris Agreement and the Carbon Neutrality Declaration⁷

The Paris Agreement and 2050 Carbon Neutrality are the basic principles of the Act, and the realization of these principles is clearly stated as a goal. By stating that goal and giving it legal binding force, it is expected that

³ <https://www.japaneselawtranslation.go.jp/ja/laws/view/4479>

⁴ Refers to business operators whose aggregate energy usage amount at all offices totals 1,500 kl/year or more.

⁵ Refers to (i) specified freight carriers under the Act on Rationalizing Energy Use (the “Energy Savings Act”), (ii) specified air carriers under the Energy Savings Act, (iii) specified consignors under the Energy Savings Act, (iv) consignors that are certified managing and supervising consignors or management-related consignors under the Energy Savings Act and have freight carriers transport freight volume of 30 million ton-kilometers/year or more, and (v) cargo-passenger carriers that are certified managing and supervising cargo-passenger carriers or management-related cargo-passenger carriers under the Energy Savings Act and have total transportation capacity of 300 cars or more.

⁶ Refers to business operators whose aggregate emissions amount at all offices total 3,000 tons or more in terms of CO₂ per type of GHG and which have 21 or more regularly hired employees throughout their entire organizations.

⁷ Stated clearly in the 2021 amendment.

ongoing efforts toward carbon neutrality will be promoted and accelerated.

(iii) Promotion of Renewable Energy Introduction Leading to Regional Vitalization⁸

Prefectures and municipalities are required to formulate plans and measures to reduce GHG emissions relating to their local administrative and business affairs, along with other measures. These plans enable prefectures and municipalities to create systems to certify businesses that contribute to efforts like local decarbonization and to complete the relevant legal procedures on a one-stop basis.⁹

(3) Climate Change Adaptation Act

The “Climate Change Adaptation Act,”¹⁰ which aims at implementing measures to prevent or mitigate damages due to the impact of climate change (“adaptation measures”), came into effect on December 1, 2018. The idea behind the enactment of this Act is that in order to tackle climate change, protect citizens’ lives and assets in the future, and strive for sustainable development of the economy and society, it is important to make efforts to adapt to climate change while at the same time making efforts to reduce GHG.

The “Act Partially Amending the Climate Change Adaptation Act and the Environmental Restoration and Conservation Agency Act”¹¹ was enacted on April 28, 2023, and a provision relating to the promotion of heatstroke prevention measures was added.

The important aspects of concern for investors concerning the Climate Change Adaptation Act are as follows:

(i) Formulation of Climate Change Adaptation Plan

The Act states that the government will establish a climate change adaptation plan, and that the climate change adaptation plan formulated in November 2018 was revised in October 2021. The plan aims to clarify the basic roles of national and local governments, as well as to specify basic measures to promote climate change adaptation in various fields, including agriculture, forestry, fisheries, natural ecosystems, and disaster prevention, and to promote understanding of the progress thereof. In addition, there is a plan to perform climate change impact assessments approximately every five years under this plan, and the plan is expected to be revised based on the results of these impact assessments.

Following the amendment of the aforementioned Climate Change Adaptation Act, discussed above, the climate change adaptation plan was subsequently amended to include heatstroke measures.

⁸ Stated clearly in the 2021 amendment.

⁹ The following are deemed performed: permission of development activities, and similar matters, in national parks and quasi-national parks under the Natural Parks Act; permission for excavation of land and other similar activities under the Hot Springs Act; certification of heat recovery facilities and written notifications of changes in the characteristics of sites that were once landfills under the Waste Management Act; permission for conversion of agricultural land under the Agricultural Land Act; permission for development activities in private forests and similar areas under the Forest Act; and registration of power generation uses of flowing water taken from a river, lake, and similar areas for water use (small hydropower), and other waters, under the Rivers Act.

¹⁰ <https://www.japaneselawtranslation.go.jp/ja/laws/view/3212>

¹¹ <https://www.japaneselawtranslation.go.jp/outline/68/905R427.pdf>

(ii) Formulation of Local Climate Change Adaptation Plans

The Act states that prefectures and municipalities will endeavor to formulate local climate change adaptation plans, in light of the climate change adaptation plan. It also states that, in order to promote climate change adaptation in local areas, prefectures and municipalities will endeavor to establish bases to collect, organize, analyze, and provide information regarding the impact of climate change and climate change adaptation, and also give technical advice thereon, as well as to develop systems that assume the function of local climate change adaptation centers.

(4) Green Growth Strategy

On June 18, 2021, the “Green Growth Strategy Through the Achievement of Carbon Neutrality by 2050”¹² was formulated. This strategy was formulated by the Ministry of Economy, Trade, and Industry in collaboration with relevant ministries and agencies, based on the common goal of achieving carbon neutrality by 2050 while significantly accelerating efforts toward structural changes in the energy and industrial sectors, and the creation of innovations through bold investment.¹³ In addition, the strategy specifies 14 important fields¹⁴ that are expected to grow, and provides action plans for each of them, from the perspective of both industrial and energy policies. The Strategy upholds an ambitious goal for the country, shows a realistic path toward it, wherever possible, and aims to support companies that strive to achieve this goal.

The important aspects of concern for investors regarding the Green Growth Strategy are as follows:

(i) Creation of Green Innovation Fund

A fund of two trillion yen was created at the New Energy and Industrial Technology Development Organization (NEDO), and the government has decided to provide ongoing support, which will cover research and development and testing phases through public implementation, for up to ten years for companies and other organizations that make a commitment towards achieving specific targets. Moreover, these support programs are specifically aimed towards sectors where policy effects are significant and which require long-term efforts to realize public implementation. As of May this year, it already had been decided to contribute up to approximately 1,830 billion yen to 19 projects over ten years, and to add 456.4 billion yen to the initial budget for 2023, suggesting that the fund is being used in a strategic manner.

(ii) Introduction of Tax System to Promote Investments in Carbon Neutrality

Based on the system to approve plans pursuant to the Act on Strengthening Industrial Competitiveness, it was decided to implement measures involving tax credits of up to 10%, or special depreciation of 50%, for (i) production facilities for products with a large decarbonization effect, and (ii) introduction of facilities that

¹² https://www.meti.go.jp/english/press/2021/0618_002.html

¹³ https://www.meti.go.jp/english/policy/energy_environment/global_warming/ggs2050/index.html

¹⁴ Includes renewable energy business, including offshore wind generation, hydrogen and fuel ammonia business, automobile and storage cell industry, and semiconductor and telecommunications industry.

balance decarbonization in the production process and other processes with enhancement of added value. Application of this tax system requires certification of the business adaptation plan pursuant to the Act on Strengthening Industrial Competitiveness by the relevant ministries, agencies, and other organizations with administrative jurisdiction over the business. The application of this tax system ends at the end of fiscal 2023.

(iii) International cooperation

The Strategy lists international cooperation as a topic and aims to lead discussions held during international cooperation efforts or multilateral and bilateral international negotiations by actively getting involved in rule-making and proposing the formulation of standards and criteria. In particular, the Strategy clarifies that the Japanese government will present a wide range of solutions to Asian emerging economies and similar entities for moving toward decarbonization from various perspectives, including those relating to finance, technical support, and human resources in areas such as renewable energy, CO2 capture, nuclear power, hydrogen, biofuel, and decarbonization of fossil fuels, while also cooperating with international institutions, such as the International Energy Agency (IEA) and Economic Research Institute for ASEAN and East Asia (ERIA).

(5) Grand Design and Action Plan for a New Form of Capitalism, 2023 Revised Version

On June 16, 2023, the Japanese government formulated the “Grand Design and Action Plan for a New Form of Capitalism, 2023 Revised Version,”¹⁵ as a new growth strategy. The Grand Design and Action Plan discusses “GX and energy security” and clearly states that under the “Basic Policy for the GX Realization,” the government will advance simultaneous efforts to realize a stable energy supply, strengthen its industrial competitiveness, improve its economic growth and decarbonization through the realization of GX.

Specifically, the Grand Design and Action Plan has a number of objectives, including but not limited to, the promotion of energy conservation, the transition to non-fossil energy, making renewable energy a main power source, promoting the introduction of hydrogen and ammonia as decarbonization efforts toward GX on the fundamental premise of securing a stable supply of energy, full-fledged operation of the “emissions trading system”, the expansion of green finance and efforts to foster an international understanding of transition finance as efforts to realize and implement the “Growth-Oriented Carbon Pricing Plan.”

3. Regulations on the Disclosure of Corporate Information

In recent years, more interest has been taken in the disclosure of information on how companies are responding to climate change.

Under Japan’s Corporate Governance Code, as revised in 2021 (“CG Code”), listed companies are required to consider further ways to address sustainability issues in a positive and proactive manner, and to develop basic policies to implement their own initiatives, from the perspective of increasing corporate value over the mid-to-long term (CG Code Supplementary Principles 2.3.1 and former clause of 4.2.2). Companies also are required to develop governance systems to support the overall initiatives and to enhance the disclosure of information relating to sustainability efforts when proceeding with specific initiatives based on the policy. In particular,

¹⁵ https://www.cas.go.jp/seisaku/atarashii_sihonsyugi/pdf/ap2023en.pdf

companies listed on the Prime Market also should enhance the quality and quantity of disclosures based on the Task Force on Climate-Related Financial Disclosures (TCFD) or an equivalent framework (CG Code Supplementary Principle 3.1.3).

Under these circumstances, a revision to the Cabinet Office Ordinance on the Disclosure of Corporate Affairs ("Revised Disclosure Ordinance") was promulgated and came into effect on January 31, 2023, and information on sustainability, including responses to climate change, must now be disclosed in annual securities reports, which are statutory continuing disclosure documents for listed companies and other similar entities. Below, is an overview of the Revised Disclosure Ordinance and the movement to establish domestic rules for IFRS Sustainability Disclosure Standards.

(1) Revised Disclosure Ordinance

In order to enhance the disclosure of sustainability information in annual securities reports, in accordance with the Revised Disclosure Ordinance, a new section of the annual securities report, titled "Sustainability Approaches and Initiatives" was established, from the perspective of providing investors with core sustainability information necessary for investment decisions in an easy-to-understand manner.

All companies that submit annual securities reports are required to describe "Governance" and "Risk Management" efforts related to sustainability, from the perspective that it is necessary for them to have a framework by which to recognize sustainability information, and to determine its importance, based on the company's business type, business environment, impact on corporate value, and other factors. In addition, based on a determination of materiality through the framework of "Governance" and "Risk Management," each company is required to disclose its "Strategy" and "Metrics and Targets" related to sustainability.¹⁶

In principle, the Revised Disclosure Ordinance does not require the disclosure of information on individual sustainability issues, and also does not have provisions that directly require the disclosure of information on responses to climate change. However, disclosure through the general reporting framework, as described above is required, as one of the sustainability information efforts. Specifically, each company is required to disclose "Governance" and "Risk Management" efforts, and if it determines that it is important to respond to climate change under those frameworks based on the company's business type, business environment, impact on corporate value, and other factors, it also is required to disclose its "Strategy" and "Metrics and targets."

(2) Movement to Establish Domestic Rules for IFRS Sustainability Disclosure Standards

On June 26, 2023, the International Sustainability Standards Board (ISSB), which was established within the IFRS Foundation, the body that sets the International Financial Reporting Standards (IFRS), issued the IFRS S1 "General Requirements for Disclosure of Sustainability-related Financial Information" and the IFRS S2 "Climate-related Disclosures" (collectively the "IFRS Sustainability Disclosure Standards").

¹⁶ Under the Revised Disclosure Ordinance, not all companies that submit annual securities reports are required to disclose a "Strategy" or "Metrics or Targets." However, the guidelines issued along with the Revised Disclosure Ordinance state that even if a company decides not to include a "Strategy" or "Metrics or Targets," after determining their importance, it is expected to disclose the determination and the basis for the determination, as an effort toward desirable disclosures.

The details of the IFRS Sustainability Disclosure Standards are planned to be incorporated into domestic rules for statutory disclosures in the future. The Sustainability Standards Board of Japan (SSBJ), which was established under the Financial Accounting Standards Foundation (FASF) to develop specific domestic disclosure standards, has announced its intention to issue an exposure draft by the end of fiscal 2023 (by March 31, 2024 at the latest) and to finalize the domestic disclosure standards by the end of fiscal 2024 (by March 31, 2025 at the latest).¹⁷

The specific details of the domestic disclosure standards will be developed in the future, and the IFRS Sustainability Disclosure Standards provide more specific disclosures of climate-related risks and opportunities, for example, disclosures of GHG emissions, including Scope 1 (direct GHG emissions by business operators), Scope 2 (indirect emissions associated with the use of electricity, heat, and steam supplied by other companies), and Scope 3 (indirect emissions other than Scope 1 and Scope 2 (emissions by other companies related to the activities of the business operator)), and it is expected that domestic rules for these will be established.

4. Conclusion

As stated above, like other countries and regions, Japan has been putting various comprehensive policies and regulations into place to respond to climate change and establishing nationwide policies for these initiatives. Among these regulations, regulations related to disclosures of corporate information are currently being developed and these will have a material impact on companies. Since it is expected that these policies and regulations will be developed in tandem with regulations in each country and region, investors who intend to engage in economic activities in Japan need to focus, in particular, on the development of these policies and pay close attention to ongoing regulations in Japan. We intend to provide an update on this situation as further details become available.

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¹⁷ https://www.asb.or.jp/en/wp-content/uploads/news_release_ssbj_20230302_e.pdf