



Current Trends and Challenges in Sustainability Reporting Practices in Japan - Literature Review

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Abstract The purpose of this study is to clarify current trends and challenges in sustainability reporting practices in Japan through a literature review. Sustainability reporting has developed since the 1990s in Japan and, currently, sustainability reporting practices have been partly replaced by integrated reporting practices. However, there is a dearth of literature regarding the evolution of these reporting practices in Japan versus other parts of the world. The extant comparative literature covers some social issues, including issues of labour practices, but comparisons of the situation in Japan to Europe or the U.S., for example, are limited. It could be argued that there have been three main challenges in the way of improving the quality of such practices and these remain unaddressed with the transformation to integrated reporting. Therefore, to explore the possibilities for improvement of these practices regardless of disclosure media, this study evaluates four approaches: enhancing companies' voluntary efforts, recognition of economic incentives, facilitating discipline of capital markets, and institutionalisation of disclosure of sustainability information. In conclusion, it can be meaningful to introduce a mandatory reporting system for stakeholders, although a careful consideration is required as to whether the reported information is accurate, clear, and useful.

Key words sustainability reporting, corporate social responsibility (CSR), voluntary disclosure, integrated reporting, environmental, social, and governance (ESG)

September 30, 2017 accepted

I Introduction

Over the past few decades, a considerable number of studies have been carried out on the sustainability reporting practices of Japanese companies. Some of notable studies (e.g. Cooke 1991; Kozuma and Umezawa 1995; Kokubu et al. 2002; Hirayama et al. 2002; Miyata 2004; Iwata et al. 2008; Ministry of the Environment 2017a) undertaken since the 1990s suggest particular trends and different challenges with respect to the practices. In addition, a survey conducted by the Ministry of the Environment of Japan (2017a) indicates that 1160 confirmed sustainability reports were issued in 2008 and about 44% of the sampled companies published reports in 2012. Currently, listed companies are increasingly issuing integrated reporting instead of sustainability reporting. However, it must be stressed that, in Japan, there have been few studies that conducted comprehensive surveys covering sustainability reporting practices of Japanese companies, and moreover, there have been very few studies adopting a positivist approach and using a statistical methodology in this field (Miyata 2004; Iwata et al. 2008) compared to studies in other countries. Therefore, there is limited discussion concerning the trends and challenges of such practices. The purpose of this research is to examine the issues regarding a lack of adequate sustainability information disclosure and explore useful approaches to improve the quality of sustainability reporting practices. Some literature indicates the concern that such practices have become outdated in Japan and whether there can be any possibility for improving the quality of such practices in Japanese companies. As such, it is worthwhile to organise the previous literature and to reconsider the issues regarding sustainability reporting practices. In addition, it can be valuable to evaluate different approaches improving sustainability information disclosure because such analysis can provide an important foundation for not only improving sustainability reporting practice itself, but also political analysis regarding costs and benefits of disclosure of environmental, social, and governance (ESG) information within companies' regulatory filings in terms of risk information for investor protection and enhancement of the transparency of capital markets.

This study consists of the following sections. The next section describes the research methodologies. In section 3, the development of sustainability reporting practices in Japan is analysed. In section 4, the current trends of the practices are examined. In section 5, different challenges with the identified practices are explored. In section 6, four approaches addressing the challenges are discussed, and in the final section, the conclusion is provided.

II Research methodologies

This study adopts a literature review in order to reveal and organise general developments and trends, challenges, and approaches for improving the quality of sustainability reporting in Japan. In this section, four aspects of the methodologies used in this study will be presented, namely, the basic terminology used in this study, research questions, how to select literature for reviewing for this study, and then theories underlying sustainability reporting practices.

1 Basic terminology

The starting point of any discussion for sustainability reports is the concept of sustainability as ‘the ability to make development sustainable to ensure that it meets the needs of the present without compromising the ability of future generations to meet their own needs’ (WECD 1987). In this sustainability context, there are different stakeholders who pursue different economic, environmental, and social interests. Organisations, including companies, can disclose sustainability information in an attempt to meet the information demand derived from stakeholders’ interests. Therefore, the potential objectives of sustainability reporting should include increasing transparency, enhancing brand value, controlling reputation, demonstrating legitimacy, benchmarking against competitors, providing signals of competitiveness to markets, motivating employees, developing internal information systems and processes, and enhancing companies’ own sustainability performance (Hahn and Kühnen 2013).

It should be emphasised that there are different concepts of corporate social responsibility (CSR) in the literature. In European contexts, CSR is defined as

'the responsibility of enterprises for their impacts on society' (European Commission 2011, p. 6). By contrast, in the Japanese context, the idea of companies' impacts on society is not emphasised. For example, Keidanren (2010) defined CSR as the responsibility to respond to stakeholders' expectations and gain their trust through companies' commitment to securing consumer safety and environmentally conscious activities and dialogue with a wide range of stakeholders. Judging from the above, the differences of concepts between contexts can be assumed to result from the varying awareness of industries regarding business impacts on society.

Furthermore, though originally sustainability and CSR have had different meanings, it is likely that they can be considered as consistent concepts in terms of a literature review of company disclosure of environmental and social information (Hahn and Kühnen 2013). Moreover, it is generally agreed that both sustainability and CSR reporting are expected to facilitate engagement with stakeholders and to identify material sustainability risks. These functions of the reporting practices are regarded as one of the important elements of accountability and also can contribute to building public trust for those companies that disclose their environmental and social information. In order to meet the needs of companies and other stakeholders, it should be stated with some emphasis that this information should be material and cost-effective to collect (Hahn and Kühnen 2013).

Finally, it is widely accepted that integrated reporting is a current concept that connects traditional financial information and sustainability information in a single report in order for companies to provide a holistic view of value creation to both management and stakeholders (KPMG 2011). However, it is important to bear in mind that the concept of integrated reporting is likely to emphasise strategic aspects and future prospects.

2 Research questions

The primary research objective of this study was to understand and present an overview of the research focusing on current issues of sustainability reporting practices in Japan through a literature review. To achieve this objective, the following research questions were posed: First, what are the general developments of sustainability

reporting practices in Japan, and how do these developments relate to relevant reporting guidelines in the extant literature? Moreover, what are the characteristics of the reporting identified by the extant literature? Second, what are the general trends of this reporting as determined by the extant literature? Third, what are the current challenges for improving the reporting practices in Japan emphasised by the extant literature? Through the literature review process, eventually, it was found that a limited number of studies have applied a positivist approach to address the issues using statistical and comprehensive research methodologies or have been published in English. In order to shed light on this research field, as well as to analyse the specific determinants of sustainability reporting in Japan, this study pursued an additional research question to explore the literature on approaches to improve the quality of sustainability reporting: what are some approaches to addressing these challenges? Which approach is most valid for the aforementioned challenges? Finally, in this study the emphasis is on the international trends and contexts.

3 Selected literature

The practical screening criteria to select relevant literature are described. Relevant literature has been selected utilising the CiNii (Scholarly and Academic Information Navigator) database service provided by the National Institute of Informatics (NII) in Japan because of its extensive coverage of academic journals published in Japan. A thorough selection of relevant academic articles within three decades was made from the database utilising the relevant keyword research method. In addition, screening criteria for the selection from the database were determined by focusing on particular terms, including sustainability and CSR in terms of information disclosure and reporting practices, rather than CSR activities and their performance. Moreover, Google Scholar was used because of its selection of articles published outside of Japan. The keyword 'Japan' was added to find relevant articles.

4 Theories underlying sustainability reporting

For the discussion of developments and challenges of sustainability information

disclosure, it is important to research topics as to what motivates the company to disclose information. To date, in this research field, it is widely accepted that stakeholder theory, legitimacy theory, and institutional theory have been utilised extensively in the academic literature. Tanaka (2013) points out that, outside of Japan, many academic studies explain the motivations for environmental reporting utilising different theories, including those aforementioned. In comparison to the above trends, it is emphasised that, in Japan, researchers' interests tend mainly to include the change of information needs and how the content of sustainability reporting allows outsiders to make decisions. Moreover, it should be stressed that most research in this field is aligned with the interests of practical businesses (Tanaka 2013). However, there is some, although limited, Japanese research that adequately explains companies' motivations by using the aforementioned theories regarding corporate reporting behaviour. The first point to notice is that some studies try to explain the motivation and characteristics of corporate reporting disclosure behaviour using stakeholder theory. The theory argues that managers need to perceive shifts in situation amongst internal and external stakeholders, and organisations should be managed in the interests of all stakeholders (Laplume et al. 2008). From this viewpoint, environmental information can be regarded as strategic information disclosure to meet the needs of stakeholders. The empirical study by Kokubu et al. (2012), focusing on investors and final consumers as stakeholders, revealed that Japanese companies do not disclose their sustainability information along with stakeholder needs. However, it is important to bear in mind that this theory cannot provide plausible reasons for the undisclosed behaviour of companies.

Second, legitimacy theory has been evidenced in some literature. It has been discussed that legitimacy theory explains that companies engage in environmental information disclosure in order to ensure their legitimacy. In addition, legitimacy can be defined as a condition that exists when the values of the organisation and the values of the society to which the organisation belongs are in harmony (Lindblom 1994, p. 2). It is emphasised that a legitimacy gap refers to a gap between the values of the organisation and those of society. In order to resolve the legitimacy gap, it is necessary for companies to ensure legitimacy for the survival of the organisation

Current Trends and Challenges in Sustainability Reporting Practices in Japan - Literature Review (Kawahara) (Deegan 2007). Based on the concept of legitimacy, Kozuma and Horie (2008) analysed the sustainability information disclosure of Japanese companies, focusing, in particular, on strategies using negative information. Moreover, Miyazaki (2013) focused on the emotional aspects of legitimacy and reputation concepts, explaining the motivation factors for corporate environmental disclosure and stressing that reputation is influenced by corporate CSR.

Finally, it can be stressed that institutional theory can provide a reason for the spread of sustainability reporting in Japan. According to the theory, the organisation field can be defined as a concept that represents an aggregate of influential relationships in which an organisation is related to a common production activity as a whole, including tendencies generated by a group of organisations that supply similar services and commodities and government organisations (DiMaggio and Powell 1983). From the institutional theory perspective, it is worthwhile to point out that companies conducting sustainability reporting do not necessarily have a business rationale, but rather, by doing so, they respond to institutionalised expectations of their environment (Meyer and Rowan 1977, Hahn and Kühnen 2013). Moreover, it is interesting to note that the reporting quality would be levelled over time because of institutional isomorphism (DiMaggio and Powell 1983). The empirical research by Komura (2009) identified that companies issue CSR reports as a means of legitimation against external factors, including pressure generated from an institutional environment derived from mainly organisational fields.

Although each of these theories has its own characteristics and can provide particular perspectives for explaining companies' activities, some theories utilised in the literature seem to be not always successful in explaining the actual sustainability information disclosure activities of Japanese companies. It is noteworthy that one of the reasons for this situation is the fact that these theories tend, to a certain extent, to overlap. In addition, because of a lack of comprehensive theoretical reference points, it is discussed that research regarding sustainability reporting provides diverse and inconsistent results (Hahn and Kühnen 2013). Through reviewing literature focusing on Japanese sustainability reporting practices, the important point to consider is that most literature seems to poorly utilise or not address the aforementioned

theories. Underlying this situation, it must be noted that it is necessary to further try to adopt specific theories for particular cases in order to provide better explanations as well as conduct empirical research based on actual companies' practices. It can also be considered necessary to develop new particular theories on sustainability information disclosure for practices in Japan (Kawahara 2016). In conclusion, the past studies have not yet reached a definite conclusion as to the theories in this field and there still remains controversy concerning the theories.

III Development of sustainability reporting in Japan

1 Early stage of development of sustainability reporting

Certain literature may provide interesting answers as to what the early stage of development of sustainability reporting in Japan looked like. It must be pointed out that the origins of this reporting can be traced back to the 1980s' corporate social reporting. As Cooke (1991) observed, in 1988, when Japan had the second largest stock exchange in the world, the sampled 48 Japanese companies disclosed voluntary items in their annual reports, which were written in English. His analysis revealed three key points: (1) the larger the companies, the more they disclosed; (2) listed companies disclosed more than unlisted companies; and (3) companies in the manufacturing industry, which had driven Japanese economic growth since the Second World War, disclosed more than companies in other industries (Cooke 1991).

In Japan, during the initial days of development of environmental reporting, most reports focused mainly on environmental information. Moreover, companies that disclosed environmental information seemed to recognise their reports as a medium for voluntary advertisement. Okuyama (1992) described these practices where companies belonging to the industries in the fields of steel and metal, chemical and pharmaceutical, and oil, disclosed their environmental information through their brochures for advertisement. It has been found that, in the early stages of environmental reporting in Japan, these issues were strongly influenced by industries rather than the government (Kozuma and Umezawa 1995). It should

be noted that the aforementioned course of development of sustainability reporting in Japan is similar to the international historical perspective analysed by (Hahn and Künen 2013). However, recently, little attention has been given to such historical analysis in literature in Japan.

2 Environmental reporting guidelines

It is widely accepted that one of the important factors that caused an increase in the number of Japanese environmental reports may be the guidelines published by the Japanese government (Hirayama et al. 2002; Miyata 2004; Iwata et al. 2008; Isogai and Tahara 2015). In 1997 the Agency of the Environment (currently, the Ministry of the Environment) issued the ‘Environmental Reporting Guideline’, readily understandable steps on preparing environmental reports (Ministry of the Environment 1997). Additionally, the Ministry of Economy, Trade, and Industry issued the ‘Environmental Reporting Guideline 2001’, emphasising stakeholders. In 2003, which is known as ‘the first year of corporate social responsibility’, implicit in the context of the ‘Fundamental Plan for Establishing a Sound Material-Cycle Society’ decided by the Cabinet, was the promotion of the preparation of environmental reports by Japanese companies, which subsequently led to the development of sustainability reporting as well as an increase in the number of issuing companies (Tanaka 2013; Isogai and Tahara 2015).

3 Some characteristics of sustainability reporting

Some notable relationships between disclosure and companies’ attributes can be observed with respect to the companies that issue sustainability reports. First, research evidence suggests that sales revenue is relevant with 83% of the companies with sales of more than 100 billion yen disclosing their environmental information to the public (Ministry of the Environment 2007a). It is evident from previous research that companies that are larger and closer to consumers (Kokubu et al. 2002), are strongly supported by stockholders and investors (Kokubu et al. 2012), and are more involved in activities related to the environment (Nishitani 2014), tend to disclose more of their environmental information. Moreover, it has been

observed that the more companies publish environmental reporting, the higher their stockholders' value; this tendency is stronger when third party evaluations improve in terms of credibility of disclosed information (Nishitani et al. 2012). However, few attempts have so far been made at international comparisons on the aforementioned relationships.

Second, in terms of report titles, it is worthwhile to state that Japanese sustainability reporting has unique aspects. The important point to observe based on the survey is that a limited number of reports were entitled 'Sustainability Report' (9%) in 2002 (Miyata 2004). In addition, it can be seen that in 2008, reports were titled 'Environmental Social Report' (35%), 'Environmental Report' (34%), and 'CSR Report' (24%), but the title 'Sustainability Report' (7%) still remained rare (Iwata et al. 2008). The title for corporate social reporting was observed to converge toward 'CSR Report' (Kozuma 2008), indicating a unique Japanese trend. Judging from the above, the question now arises whether the concept of sustainability as well as CSR has been adequately understood by companies.

Third, given the information from a survey, with respect to the media used for the sustainability reports, the combination of paper medium and website (54%) is more popular than website only (30%), and 48% of the reports are also issued in English (Toyo Keizai Shinposya 2017). Moreover, another survey suggests that 82% of the companies publishing on paper medium also publish environmental information on their website (Ministry of the Environment 2007a). However, it should be not overlooked that the English versions of the reports were literal translations from Japanese with expressions typical to the Japanese context, rather than effective translations to convey the actual meaning, which can be difficult for non-Japanese speakers to comprehend, and therefore, Japanese companies' efforts relevant to CSR could be undervalued by them (Akabane 2017). Judging from the above, the question that needs to be considered for the companies in question is who their stakeholders are and how they can adequately address these different stakeholders.

IV Current trends

1 Decreasing voluntary disclosure

It can be emphasised that recently the number of published environmental reports has decreased and some of these environmental reports have been combined into annual reports, which, in Japan, are voluntarily issued by companies for the purpose of investor relations in the form of integrated reporting. According to the Ministry of the Environment (2017a) survey, the percentage of companies making a voluntary disclosure of the reports reached a peak in 2002, as 44% (listed companies 71%; unlisted companies 32%), and then gradually decreased. In addition, it is noteworthy to mention that in order to increase the number of reports as well as to improve the reporting quality, the Ministry of the Environment has begun the process for revising their guidelines, specifically focusing on environmental reports, rather than covering different ESG information (Ministry of the Environment 2017b). Here one gets a glimpse of the issues concerning companies' arbitrage of disclosure based on the voluntary disclosure system in Japan.

A further point needing clarification is that the decrease in the disclosure of environmental information leads to a quantitative challenge for Japanese sustainability reports. According to a survey, between 2001 and 2002, the number of reports that disclosed non-environmental items increased by 20% (Miyata 2004). Research evidence suggests that, since 2003, the significance of non-environmental information other than the environmental information has been recognised by Japanese companies, and the volume of quantitative information on environmental information presented in their reports has decreased; there is concern that this trend has promoted qualitative deterioration of sustainability reporting practices (Kozuma 2007). It was found that, by 2007, in addition to the notable shift from environmental reports to CSR reports in many Japanese companies, environmental information disclosure practices drastically decreased, information deteriorated, and reports were criticised for diluting their content (Editorial department and Murakami 2007).

This trend offers the key to an understanding of the very heart of the problem

of Japanese reporting practices, namely, that this decreasing trend has revealed a weakness of voluntary disclosure in Japan. First, it is suggested that sustainability reports were generally recognised as one of the vehicles for voluntary disclosure, merely created with reference to some guidelines for preparation of reports, and because the companies' reporting practices were not driven by stakeholder pressure, their motivation for reporting could be ambiguous (Editorial department and Murakami 2007). Second, a criticism exists that sustainability reports have recently been 'digest oriented' and 'PR oriented', where the explanation provided is insufficient compared with that in similar reports in Europe, and moreover, that it is doubtful whether both the corporate and stakeholder sides actually use the information disclosed in these reports (Kokubu 2015).

Third, according to a survey, currently, companies that disclose environmental information to the public (2012, 53.0%; 2015, 44.9%) have decreased and the number of non-disclosing companies are increasing (2012, 40.5%; 2015, 47.2%) (Ministry of the Environment 2017a). It should be noted that the reason provided for this is that the disclosed information is 'specifically not requested' (56%) (Ministry of the Environment 2017a). However, the evidence in the survey suggests that 30% of the sampled companies were in favour of mandatory disclosure of important environmental information in regulatory annual reports (Ministry of the Environment 2017a). The key is that such companies would prefer a mandatory reporting system to a voluntary one. It will be useful to keep these points in mind when the challenges of reporting practices are considered.

2 Impact of integrated reporting

It cannot be emphasised too strongly that the current trend of a shift from CSR reports to integrated reports could be controversial because such shifting potentially leads to deterioration in the quality of sustainability information disclosure. KPMG (2017) refers to the fact that the number of integrated reports in Japan has increased from 26 in 2006 to 279 in 2016, and 50% of the companies in the 'Nikkei 225 Index' and 37% in the 'JPX 400 Index' published their integrated reports. In addition, it is interesting to observe that companies with a strong influence

from shareholder investors are issuing integrated reports earlier (Nishitani and Kokubu 2016).

However, the point that there is a possibility of a reduction in the volume of ESG information disclosure under the transformation to integrated reporting deserves explicit emphasis. It is noteworthy to consider that according to an International Integrated Reporting Committee (IIRC) discussion paper (IIRC 2011, p. 6), a sustainability report should exist if it provides ‘reference points’ of information handled by other communication means (Yamaguchi 2014). However, in practice, it can be observed that companies that issue integrated reports tend not to issue sustainability reports; they merely transform from sustainability reporting to integrated reporting rather than proactively collecting relevant data to the same extent as prior to the transformation (Yamaguchi 2014). Furthermore, this observation helps explain why this trend of a shrinking volume of ESG information is criticised because the trend is similar to the declining volume of environmental information disclosure when the number of CSR reports began to increase in 2003, when CSR reports were transformed from environmental reports (Yamaguchi 2014). Here, what is important to consider is if the shift to integrated reporting is more prevalent in the future, how do we make companies disclose their sustainability information to keep the quality without eliminating companies’ arbitrariness?

V Current challenges

1 Concept, purpose, and awareness

It can be accurate to say at the outset that, in Japan, the sustainability reporting practices face many different substantial challenges. Among these different challenges, it is possible to build up three main arguments, namely, misunderstanding of concepts and the purpose of sustainability reporting practices and a lack of awareness; a dearth of respect for reporting standards; and weak regard for stakeholder issues. First, it cannot be emphasised too strongly that the reporting does not necessarily address a comprehensive disclosure of companies’ sustainability information because of a misunderstanding of the concept of CSR. It is debatable that the con-

cept of CSR tends to be recognized as an ‘activity to prevent social and environmental problems, including environmental conservation at workplaces, occupational safety and health, and social contribution activities’; this concept is narrow compared to the concept of ‘corporate sustainability’ in Europe (Isogai and Tahara 2015).

Second, as for the purpose of sustainability reporting practices, it has been argued that such practices can be seen as a part of a company’s information strategy, and the information disclosed can be arbitrarily selected by management. Kozuma and Horie (2008) critically pointed out that when negative information is disclosed in sustainability reports, companies tend to use their information strategy to intervene to make arbitrary information selections. The evidence in the survey suggests that when there is negative information, unless the information selection criteria are clear, it does not contribute to the reliability of the reports (Kozuma and Horie 2008).

Similarly, there is not rebuttal for the argument that non-comprehensive disclosure practices of Japanese companies can result from unwillingness to consider disclosing companies’ information, which addresses their negative information. In particular, highlighted disclosure tends to emphasise favourable issues; the reluctance to disclose the negative environmental and/or social impacts of business activities casts a shadow on their reporting. Therefore, it is criticised that the overall picture of the company becomes invisible for the readers, its report seems to be just merely a public relations piece, and eventually readers would not try to evaluate the company by using its sustainability reporting contexts (Yamaguchi 2014).

Furthermore, it is an open question that the concept of ‘creating shared value’ (CSV) introduced by Porter (2011) could have a controversial effect. It appears that disclosure utilising the concept of CSV, which is highly compatible with strategic CSR, could change the substantive purpose of sustainability reporting, which was originally meant to explain the responsibility for social impacts resulting from business activities (Yamaguchi 2014).

At the same time, it can be discussed that the idea of disclosure of sustainability information in regulatory annual reports may be poorly understood by companies. A survey by Nagai (2014) demonstrated that among more than 3000 listed publicly

traded Japanese companies, only about 100 companies disclosed their occupational health and safety issues in regulatory annual reports, namely, ‘Yuka Syoken Houkousyo’, which is similar to 10-K filings in the United States. Moreover, the research conducted by Nagai (2014) stressed that such disclosure is limited in the reports, indicating that companies have a negative attitude toward disclosure of these issues. In addition, the research argued that because these were not yet mandatory disclosure items in Japan, most Japanese companies believed these issues were related to labour customs or legal regulations rather than financial performance, and hence would not be relevant to investors. Moreover, it is distinctly discussed that there has been a poor focus on these issues in Japan, and arguments with regard to CSR issues in the area of labour practice are poor (Nagai 2014).

It is worthwhile to examine the relevant impact on society of the identified challenges. For example, given the absence of a clearly defined concept of human rights, there is usually a reluctance to discuss labour issues in Japan among individuals and the media. The latter’s coverage of issues depends on discussions among managers in the industry, who themselves tend to avoid such topics. Although ‘karoshi’, the phenomenon of excessive work leading to death, has recently gained traction following the death of an employee in one of the largest advertising firms (North and Morioka 2016), unpaid workers may still continue to be neglected in many work places in Japan. Consequently, although some information can be disclosed by a company in question in an ad hoc manner, others’ disclosure may not change as much as expected by stakeholders.

Third, with regard to awareness within companies, in recent years, it seems that management’s awareness of the purpose of disclosing environmental information is also decreasing. A survey conducted by the Ministry of the Environment (2007a) analysed this decrease as: ‘to fulfil social accountability’ (2015, 90.2%; 2017, 86.9%), ‘to inform our business partner about their efforts’ (2015, 74.3%; 2017, 65.0%), and ‘to be used as investment and loan information’ (2015, 38.9%; 2017, 32.5%) (Ministry of the Environment 2017a). In keeping with the rationale for the aforementioned change, some large companies that caused major accidents or corporate scandals have stopped publishing their sustainability reports, which was criticised as ‘a re-

grettable decision' (Yamaguchi 2015). It would be better to say that because of a dearth of solid understanding of the responsibility of business regarding business impacts on society, management can poorly understand the rationale of reporting practices.

Before turning to the second challenges, it cannot be emphasised too strongly that, in Japan, the concept of sustainability as well as CSR, for many companies, has still been misunderstood and therefore, the purpose of such reporting practices seems to be still considered mostly artificial and carried out poorly by an ad hoc management, not carefully considering their potential and existing impacts on society. This argument is closely relevant to the difficulties of voluntary disclosure systems in Japan.

2 Reporting standards

It is worthwhile examining the second challenges, namely, the problem of non- or poor compliance of international standards relevant to sustainability reporting practices, including the GRI guidelines as well as ISO26000. The first point to consider is that there are gaps in terms of the level of application of international standards relevant to companies' reporting practices. Prevailing international standards appear to be the Global Reporting Initiatives (GRI) guidelines and ISO26000, which closely focus on the impacts of companies' business on society and the environment. However, a small number of reports mention negative impacts related to companies' business activities, and therefore, many third-parties who provide commentary on sustainability reports published in 2013 encouraged companies to increase disclosure of the shadow impacts caused by their activities (Yamaguchi 2014).

Second, it is worthwhile to clarify the fact that the disclosure of social information within Japanese sustainability reporting is generally low, which can be seen as a specific weakness. A survey by Kawahara and Irie (2015) identified that among sampled companies, a limited number of companies disclosed information with regard to human rights, gender, discrimination based on worker classification, corporate corruption, and corporate penalties although the GRI guidelines encourage disclosure of these issues. Moreover, the survey emphasised that these issues, which companies

do not want to disclose, very much suggest overall weakness in Japanese corporate social disclosure (Kawahara and Irie 2015).

Third, it is noteworthy to mention that because the culture, value, and philosophy of social responsibility investment have not been fostered in Japan compared to the United States and Europe, little information is available on occupational health and safety (Nagai 2014).

Fourth, an interesting trend in Japan is that the guidelines set by the Ministry of the Environment are mainly referenced in reporting practices. According to the survey conducted by Miyata (2004), since the GRI issued the Sustainability Reporting Guidelines in 2000 and 2002, 100 sample companies applied the GRI guidelines (62%) and these companies clearly stated the importance of sustainability within their reports (44%). However, the result of the survey pointed out that the GRI Guidelines would be poorly acceptable and considered ineffective within Japan in the future (Miyata 2004). Moreover, the survey conducted by Iwata et al. (2008) demonstrated that among the 319 sampled companies, the guidelines from the Ministry of the Environment (79%) were more often referred to than the GRI guidelines (50%). Moreover, it must be noted that some sustainability reporting in Japan was not in accordance with the GRI guidelines. For example, the survey conducted by Kawahara and Irie (2015) pointed out that in terms of sustainability reporting, fewer of the sampled Japanese companies complied with the GRI version 3.1 than companies in other developed countries. In addition, it was also observed that the degree of compliance of listed companies' reporting with the GRI version 3.1 has a positive relationship with the degree of using the 'Core Index' of the GRI version 3.1 (Kawahara and Irie 2015).

Fifth, in terms of a better understanding of the philosophy of the GRI guidelines, it is strongly criticised that sustainability strategies and efforts are not incorporated into corporate strategies, namely, mid- and long-term corporate strategies are not included in sustainability reports, and also corporate efforts related to environmental and social aspects are merely listed within the contexts of the reports, without indicating the actual results of concrete efforts utilising measurable key performance indicators (KPIs) (Isogai and Tahara 2015).

Sixth, one may notice that that Japanese sustainability reporting tends not to comply significantly with international standards, including the GRI guidelines as well as ISO26000, although the latter does not specifically pertain to sustainability reporting. A current survey revealed that the proportion of sustainability reporting referring to ISO 26000 is still approximately one third the level of the previous survey in 2014 (Ministry of the Environment 2017a). Let us now attempt to extend the argument that even if many international guidelines are referenced by companies, the actual disclosure level may differ depending on the social values of the area in which the company conducts business (Saka 2016). In addition, the evidence in the survey conducted by Saka (2016) demonstrated that the higher disclosure items in Japan were similar to those in South Korea: the environment (Japan 84%; South Korea 60%) and labour practices (Japan 47%; South Korea 56%), and Japanese disclosure focuses on environmental issues rather than social ones to a greater extent than Korea (Saka 2016). Having observed the above, one can then go on to consider the question as to why such social disclosure is likely ignored as well as the identified international standards. In conclusion, it seems reasonable to explain that the non- or poor compliance of the aforementioned international standards implies a lack of respect for fundamental international standards, including the International labour standards (ILO) and the Protect, Respect and Remedy: a Framework for Business and Human Rights, which are highly recommended references for preparing reports. Therefore, it is not far from the truth to mention that, although there are many useful references for sustainability information disclosure practices, if under a voluntary basis, companies are free to choose arbitrarily their contents to be disclosed.

3 Stakeholder issues

One can safely state that the unbalanced recognition of stakeholders by companies may be a sign of companies' business policy itself and not directly connected to the international agenda, including the Sustainable Development Goals (SDGs). It is no exaggeration to say that there are unique features with regard to stakeholder issues addressed in sustainability reporting in Japan. First, it is criticised that

although there are different relationships with a wide range of stakeholders of companies, sustainability reporting by the companies in question utilises a unilateral, (a 'one size fits all') one sided approach to communicate to their stakeholders, and therefore some information asymmetry between the sender and the recipient remains (Miyata 2004).

Second, the argument that the recognition of a company's primary stakeholders may change their focus as well as their relationships in their reports makes sense. It is noteworthy to say that companies in other parts of the world primarily recognise their employees as the primary communications focus, rather than stockholders, investors, communities, or governmental organizations. However, Kozuma (2008) identified that, in Japan, companies in question tend to address customers in their reports, followed by their employees. Given the findings of the aforementioned survey, it is likely that the main reason sustainability reporting was introduced by Japanese companies was that companies were forced to change to be in lockstep with the external environment as well as domestic and overseas trends (Komura 2009). Moreover, the other literature suggests that sustainability reporting practices were merely an adoption of reporting in a formal way rather than a re-evaluation of companies' relationship with the stakeholders (Komura 2009).

Even if recently, some companies have disclosed their policy towards their SDGs, which focuses on different aspects relevant to improving stakeholder relationships, it is not to be denied that most of the companies would accept that they have not adequately addressed the international agenda without any specific mandatory requirement within Japan. This situation, therefore, may predict that the stakeholder relationships cannot be adequately addressed under normal business conditions.

VI Discussion: four approaches

In the preceding chapter this study pointed out three challenges. This section discusses four available approaches to address these different aforementioned challenges. Some of these approaches are extant, but they can be introduced in different companies and industrial contexts. It is important to evaluate the validity of the approaches.

1 Voluntary efforts of companies

An applicable first approach would be for companies to rebuild their own adequate systems to enhance voluntary sustainability reporting under ongoing Japanese legal requirements. The following, from the viewpoint of companies' management, may be informative, namely that the points of reconstruction of the reporting system within companies can include: (1) confirming the significance of disclosure of sustainability information, (2) establishing an information disclosure policy, (3) building communication and media strategies, (4) establishing a cross-sectional internal information collection system within companies, (5) making use of the report preparation process to penetrate and revitalise internal CSR activities, and (6) effectively utilising the report (Yamaguchi 2013).

Moreover, it could be stressed that when reconstructing the internal reporting system, the following considerations for outside companies can be useful for increasing the effectiveness of the report, namely: (1) verification of the company's CSR based on international norms, (2) utilising international guidelines from the draft stage to prepare reports, (3) grasping the social issues and social existence value of the company, (4) from the value chain viewpoint, grasping and verification the extent to which the company impacts society and the environment, especially in terms of negative impacts, and (5) basing the report on international norms while considering the history, culture, and national characteristics of the company's business activities areas (Yamaguchi 2013).

This argument makes sense given certain conditions within companies and this approach could provide companies in question with a managerial value. However, it is debatable that in order to rebuild companies' systems based on the above considerations, it may be necessary to clearly motivate companies' managers. The validity of this approach remains a matter for debate and it needs further consideration. Therefore, in the next section, it can be useful to address the perspectives of economic incentives for managers with regard to sustainability information disclosure.

2 Recognition of economic incentives

There is room for argument that it can be useful for managers and investors

to recognise the specific relationship between shareholder value and capital cost because such recognition may create economic incentive opportunities for them. Some empirical research focusing on shareholder value and capital cost in the capital market in Japan suggests that it may be economically advantageous to voluntarily disclose sustainability information. The survey conducted by Nishitani et al. (2012) observed a notable relationship between publishing environmental reports and higher shareholder value as well as the effectiveness of acquiring assurances and/or opinions from third parties in support of their reporting. Another survey also observed that companies that make positive efforts to address environmental issues and actively disclose environmental information have higher shareholder value (Nishitani 2014). In addition, the survey clarified that at one time, companies' environmental efforts had directly negative impacts on their shareholder value, but over time this influence gradually decreased and eventually became positive (Nishitani 2014). Moreover, Tanaka (2003) analysed that the shareholders' capital cost for companies that disclosed environmental reporting over long periods was consistently lower than that of other companies (Tanaka 2003).

Much can be stated about the usefulness of the recognition of these economic aspects in terms of the attention of management and investors. However, it is likely that if some managers and investors have a short-term perspective, this second approach may not always facilitate sound voluntary disclosure and depend on companies' economic situation. Therefore, the following section calls for further discussion about a third approach discipline regarding capital markets, which aims to achieve sustainable capital markets and transparency of companies' information.

3 Discipline of capital markets

For the present, it may be useful to look more closely at some of the more valid approaches based on the discipline of capital markets. A current international trend is to take a normative approach to voluntarily disclose information on social and environmental impacts within current governmental policy contexts (Cabinet office 2013, p. 16; 2014, p. 20) of seeking capital market discipline among institutional investors and listed companies. Examples of this discipline are the two market

codes that followed the policy, namely, the ‘Japan version stewardship code’ (revised in 2017) (FSA 2014; 2017) published by the Financial Services Agency and ‘Japan’s corporate governance code’ published by the Tokyo Stock Exchange (TSE 2015), were respectively issued. First, in the ‘Japan version stewardship code’ (guidance 3-3), it has been discussed that in order to properly fulfil institutional investors’ stewardship responsibilities towards the sustainable growth of investee companies, such investors are requested to monitor the companies’ business risks and opportunities arising from social and environmental matters and how the companies address them (FSA 2017, p. 12).

Second, it can be stressed that the ‘Japan’s corporate governance code’ (principle 2-3) requested that listed companies positively and proactively address sustainability issues, including social and environmental matters, as an important element of their risk management (TSE 2015, p. 11). In addition, according to the code (principle 3), listed companies are required to strive to actively provide information beyond that required by law as well as appropriately provide information in compliance with the relevant laws and regulations. In this context, information to be disclosed includes both financial and non-financial information related to business risk. In particular, it is stressed that non-financial information needs to be accurate, clear, and useful in order to serve as the foundation for constructive dialogue with shareholders (TSE 2015, p. 13).

It is important to consider that these two codes articulate that sustainability information is an important part of companies’ risk management, and therefore, the information should be voluntarily disclosed to investors without depending on laws and regulations. In addition, it can be valued that both of these codes are influential because they explicitly request capital market participants to adequately address their risks associated with corporate social and environmental matters and sustainability issues, and moreover, with relevant voluntarily disclosure information. In other words, these disciplines can add a certain value to the capital market itself from the attention of investors, which typically have long term views in their investment decisions.

However, the problem of this third approach is that these are still voluntary disciplines; the point that a legally binding approach has not yet been undertaken

cannot be emphasised too strongly. Because of the revision of the ‘Japan version stewardship code’ within just three years, there are still some limitations of this approach in terms of validity.

4 Mandatory reporting

The discussion of the validity of the mandatory approach of legislative institutionalisation, in which laws and regulations require companies to disclose specific types of sustainability information, can be useful. Some studies on laws and regulations concerning the disclosure of sustainability information in foreign countries, including Europe, the United States, and Asia (Kozuma 2005; Kawahara 2010, 2011, 2012, 2013, 2017; Nagano 2011; Kawahara and Irie 2014), considered that mandatory disclosure of sustainability information is an option in Japan. Moreover, it should be emphasised that it can be of significance to institutionalise sustainability information disclosure in companies’ annual reports prepared as legal documents. The survey conducted by Kozuma (2005) pointed out that in Europe, environmental information disclosure is being institutionalised; this is important because: (1) it provides a specific background against which the importance of corporate governance among industrial societies is increasingly recognised and capital markets are seeking information disclosure, and (2) it can be recognised as a convergence of disclosure forms and contents. It cannot be emphasised too strongly that institutionalization of sustainability information should consider all aspects of sustainability, not just environmental disclosure, but other pertinent areas such as labour matters. For example, the EU directive (EU 2014) for non-financial information covers not only environmental issues, but also labour issues. Given that social matters, including labour practices have been poorly addressed for a long time in Japan, mandatory sustainability reporting should consider them. However, it is important to discuss that there can be certain limitations even if disclosure is institutionalised within laws and regulations. For example, it can be observed that currently in Indonesia, laws and regulations with regard to disclosure of sustainability information have been articulated, but it has been criticised that these provisions are general and not addressing specific issues (Kawahara and Irie 2014), which can result in the situation in which there

is much room for management's discretion in terms of quantitative and qualitative aspects of sustainability information disclosure (Kawahara 2017).

It can be concluded that introducing mandatory reporting can be expected to directly impact reporting practices, but it is necessary to carefully consider whether the information disclosed is accurate, clear, and useful. Therefore, there is considerable validity to this approach although the other identified approaches should not be excluded.

Based on the thorough literature review as well as results of empirical surveys, it is clear that very few studies in Japan have critically evaluated these approaches. There is room for further discussion about the validity of not only the four aforementioned approaches but also others, which are not covered in this study due to space limitations. Moreover, in terms of other approaches, further research should consider including the use of ESG ratings, portfolios in ESG index funds, different international agreements and initiatives, and calling for ESG information by investors.

VII Conclusion

Although over the past few decades numerous attempts have been made by scholars to address sustainability information practices in Japan, most of studies fail to grasp the trends and challenges of such practices. This study contributes by clarifying recent trends and challenges as well as approaches addressing the challenges in the practices using a literature review.

This study consisted of the following sections: Section 1 was a general introduction. Section 2 described the research methodology, research questions, selected literature, and theories underlying sustainability reporting practices. Section 3 examined the development of the reporting, issues of environmental guidelines provided by the Japanese government, and some specific features of the reporting. Section 4 analysed the current trends indicating that integrated reporting has been replacing sustainability reporting, and examined the issues with regard to the decline of information disclosure accompanying the shift to integrated reporting. The important point to note is that though Japan's sustainability reporting has evolved since the 1980s, it appears

that currently there are signs of recession and deterioration of the quality of reporting practices. Section 5 examined three challenges facing the improvement of Japanese companies' sustainability reporting practices, namely, misunderstanding of concepts, purpose, and a lack of awareness; non- or poor compliance of international reporting standards; and unbalanced recognition of stakeholders. Lastly, Section 6 considered four approaches, namely, enhancing voluntary efforts of companies; recognising economic incentives; facilitating the discipline of capital markets; and institutionalisation of sustainability reporting in order to address the three challenges in the previous section as effective measures to improve the quality of disclosure of sustainability information.

It could be concluded that the most valid approach is to introduce a mandatory reporting system for stakeholders, although a careful consideration is required as to whether the reported information is accurate, clear, and useful. A mandatory reporting system is the only approach that can directly change companies' reporting practices and strongly influence the way of thinking of companies and investors. Even with the current reporting practices for environmental issues, social issues are likely to be still ignored. The laws and regulation with regard to environmental business practices in Japan were spawned after the era of pollution suits since the 1960's; there has not been a similar impetus for social business practices. Moreover, it is important to note that in many countries and areas across the world, recently, numerous different laws and regulations and other relevant instruments for ESG information disclosure have been increasingly established. This international trend can have a strong impact on Japanese companies' reporting practices and the establishment of relevant laws and regulations within Japan. Having suggested that, there is still a long way to go before achieving a sound level of sustainability information disclosure practices, which may be expected for different stakeholders. However, the proposal of introducing a mandatory reporting requirement in Japan is a valid argument in order to shed light on the aspects of actual or potential business impacts on society, as well as risks of companies in question for investors. Additionally, this approach would facilitate the improvement of the quality of the monitoring practices by authorities and capital markets, accompanying international

norms and agreements. Furthermore, the argument should include what type of sustainability information in mandatory annual financial reports may be useful for decisions of investors as well as authorities, who may consider the disclosure policy and facilitate the political analysis regarding the costs and benefits of disclosure of ESG information within companies' regulatory filings in terms of risk information for investor protection, and the enhancement of transparency and credibility in capital markets.

This study has some limitations in terms of literature selection as this study focuses on the practical issues of both disclosure and reporting rather than evaluation of actual environmental and social impacts resulting from companies' activities. Further research can examine the current changes in ESG information disclosure in regulatory annual financial reports of listed companies, and the comparison between Japanese and other countries' investors' perception of ESG information in these reports underlying the current trends of development of different mandatory disclosure mechanisms in different parts of the world.

Acknowledgments

This work was supported by JSPS KAKENHI Grant Number 15K03801.

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