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Directors' duties regarding climate change in Japan: 2025

What board directors need to know

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About the Commonwealth Climate and Law Initiative

The Commonwealth Climate and Law Initiative (CCLI) is UK non-profit organisation founded by the Oxford University Smith School of Enterprise and the Environment, ClientEarth and Accounting for Sustainability.

We take a multidisciplinary approach, linking existing laws, scientific research and financial evidence to examine the legal basis for corporate and investment decision-makers to address climate- and nature-related financial risks. At the same time, we apply insights from behavioural science to help these decision-makers navigate the law and fulfil their duties by translating complex legal frameworks into clear, practical and industry-relevant resources.

We collaborate with leading organisations, such as the World Economic Forum, the Law Society of Singapore, the Oxford Sustainable Law Programme, Peter A. Allard School of Law (University of British Columbia), Pollination, the World Benchmarking Alliance and the Taskforce on Nature-related Financial Disclosures.

Our Canadian partner, the Canada Climate Law Initiative, is a collaboration of the University of British Columbia and York University. It provides directors, trustees, and regulators with climate governance research and guidance so they can make informed decisions in the transition to a net-zero emissions economy. The Canada Climate Law Initiative is situated on the ancestral, unceded territory of the xwməθkʷəy̓əm (Musqueam) and is committed to working in partnership with Indigenous communities.

More information here.

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Directors' duties regarding climate change in Japan in 2025

In February 2021, the Commonwealth Climate and Law Initiative (CCLI) released *Directors' duties regarding climate change in Japan*, a report authored by leading academics Dr. Yoshihiro Yamada, Dr. Janis Sarra, and Dr. Masafumi Nakahigashi. To mark its four-year anniversary, the authors have released an updated edition, ***Directors' duties regarding climate change in Japan: 2025*** (the Report).

The Report makes the following key findings:

1. **Duty to identify and manage climate risks:** Directors have an obligation to identify and manage climate-related risks and opportunities. Failure to do so could result in personal liability for not acting with due care and in the best interests of the company.
2. **Internal risk management:** Directors of large stock companies are required under statute to establish proper internal control and systems related to management of the risk of loss to the company, including climate risks. As such, climate governance[1] should be embedded in the board's risk-management strategy.
3. **Board-level responsibility:** The entire board retains legal responsibility for oversight of company efforts to identify and manage climate-related risks and opportunities - regardless of whether risk management or disclosure responsibilities are delegated to a specific board committee.
4. **Business Judgment Rule:** Courts are unlikely to defer to the business judgment of directors if they fail to conduct reasonable analysis of the relevant facts on climate-related risks and opportunities, get expert advice on climate-related risk management, and/or fail to exercise due care in respect of climate risks.
5. **Disclosure of material information:** Directors of publicly and privately held companies have an obligation to shareholders to report material financial information in their financial statements. If information is material, failure to disclose could give rise to a complaint that the directors have failed in their fiduciary duty.
6. **Climate change mitigation and adaptation expectations:** While there are no legal liabilities for directors for non-compliance under climate-specific legislation, the law in Japan creates regulatory expectations that all sectors of Japanese society make efforts to control climate change through mitigation and adaptation.
7. **Increase in litigation risk:** As companies and financial institutions experience more financial losses due to climate change, directors face an increasing risk of litigation for failure to address and mitigate these losses.
8. **International alignment of disclosure standards:** On 5 March 2025, the Sustainability Standards Board of Japan (SSBJ) issued its final sustainability disclosure standards. From this date, companies may voluntarily apply the standards. The standards are expected to become mandatory for all Prime-listed companies through a phased approach, beginning in March 2027.
9. **Nature:** Many Japanese companies have high direct dependencies on nature, estimated to be about 18% of the local stock market's capitalisation (USD 938 billion). Nature risks may constitute material financial risks that directors have a duty to oversee.

Across the globe, there is growing recognition of the material financial risks associated with climate change. In Japan, the government has formally acknowledged climate change as a significant threat to the

[1] Climate governance refers to the rules and processes an organisation puts in place to manage its responses to the risks and opportunities of climate change. The World Economic Forum and PricewaterhouseCooper have developed a set of climate governance principles to help boards and senior management consider the quality of climate governance at the organisations they oversee and identify aspects in need of development or enhancement. WEF, How to Set Up Effective Climate Governance on Corporate Boards Guiding Principles and Questions (January 2019).

sustainability of nearly all Japanese companies. The Bank of Japan has also warned that failing to adequately price climate risks could trigger disruptions across the real economy and financial system.

As the Report highlights, these risks are no longer optional but mandatory considerations for directors. Here, we summarise the Report's contents to support directors' understanding and exercise of their legal duties with respect to climate risks. This summary is not a substitute for legal advice or a comprehensive analysis of all the relevant issues. For detailed legal insights, we recommend a full reading of the Report.

Best practice guide for directors

Directors have an obligation to identify and manage climate risks and opportunities. The board may want to consider the following tips to meet regulatory requirements and market expectations:

- **Integration into board governance:** Ensure climate-related issues are **integrated into board governance, strategy, and oversight responsibilities** and are receiving **time, consideration, and focus** on the board/committee agenda.
- **Consider the risks:** Ensure climate-related issues are fully **integrated into strategic planning and oversight of risk management**, including financial and operational risk management, and that the board understands the relevant risks and opportunities for the company in the short, medium, and long term.
- **Plan for transition:** Ensure that a process is on the board agenda to start **developing a credible, coherent and comprehensive climate transition roadmap/strategy** to 2050, with **transparent net zero or reduction targets and clear interim targets** to 2030 and 2040 and within the current rolling multi-year strategic plan. Ensure there is a process for annually reporting to the board on progress to meeting the targets.
- **Assign responsibility and ensure oversight:** Ensure that **responsibility for climate risk identification, management, and evaluation is assigned** to a clearly identified management team that reports directly to the CEO and board, and that the **board has effective oversight** of that management.
- **Delegate to relevant functions:** Delegate to the appropriate committee(s) of the board the responsibility of **translating the company's long-term strategy into a structured decision-making process** for each aspect that is relevant to each committee's terms of reference. Such committees might include risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility.
- **Comply & disclose:** Ensure that **material climate-related issues are being disclosed** in accordance with legislative and regulatory requirements and, where necessary, consult with advisors.

Directors' duties in relation to climate change

Companies in Japan may choose one of three main forms of organisational structure under the *Companies Act of Japan*: (1) a Company with *Kansayaku* Board; (2) a Company with Three Committees; or (3) a Company with Supervisory Committee. All three forms of company governance structures have a board of directors.

The scope of directors' and officers' duties in Japan is set out in the *Companies Act of Japan*, the *Civil Code of Japan,* and in the companies' articles.

Directors in Japan have **three main duties**:

1. **A duty of loyalty:**[2] Directors are required to perform their duties for the company in a "loyal manner", which means that directors are required to act in the **company's best interests**.

   Applicability to climate risks: A growing number of lawyers and regulators believe that directors' duty to act in the best interests of the company **includes a duty to oversee its long-term sustainability**.[3] Where directors lack the expertise and that **expertise is not available** among the executives of the company, directors should **hire outside professional expertise** that can **support their climate-related risk management decisions** in the **best interests** of the company.

2. **A duty to comply with all laws:**[4] Directors are required to comply with all laws, regulations, ordinances, resolutions of shareholders' meeting and the company articles of association. Directors of large companies are additionally required to develop **internal controls and systems** for managing the risk of loss.

   Applicability to climate risks: Given the risks that climate change poses to companies, **climate governance** should be **embedded** in the **board's risk-management strategy**. Directors have **broad discretion** to design internal control and risk-management systems, given the **likelihood and magnitude of climate risks** to the company. Systems should be **tailored** to handle the specific climate risks the company faces, taking into account the size of the business and the potential impact of these risks.

   The board may **embed oversight** of climate risks to a specific committee. Any committee authorised must have directors that have sufficient capability to **scrutinise climate risks** (physical, transition and legal) to the company and then to **interact with management and the board to oversee and manage these risks**. The board **has legal responsibility** for the company identifying and managing climate-related financial risks regardless of allocation.

3. **A duty of care:**[5] Directors must exercise the care that a **good manager** would exercise. This duty informs the duty of loyalty and the duty to comply with all applicable laws. The **business judgment rule**, as recognised by the Supreme Court of Japan, *may* offer a **defence** to specific actions concerning the management of climate-related risks and opportunities. However, this safe harbour is limited as Japanese courts have been clear that they will **undertake a review of directors' decisions from an objective standpoint** to assess whether a director acted **unreasonably** at the time of the decision. If directors **neglect** to undertake **reasonable analysis** of the relevant facts, **fail to get expert advice** on climate-related risk management, and/or **fail to exercise due care** in

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[2] Article 355, Companies Act of Japan (Act No 86 of 26 July 2005) (Companies Act).
[3] Koichi Kusano, 株主の利益に反する経営の適法性と持続可能性 (Yuhikaku, 2018) 347-348.
[4] Articles 348,362,399-13 and 416, Companies Act.
[5] Article 644, Act No 89 of 27 April 1896, as amended; Articles 330 and 355 Companies Act.

respect of climate risks, the courts are unlikely to defer to their business judgment and could find that they have breached their duty of care.

Applicability to climate risks: Directors should act in accordance with their duty of care by **addressing climate-related risks and opportunities**.

Consequences of breaches

Directors who do not exercise their duties are **jointly and severally liable** to the company for any resulting damages, which means that where a director has breached their duty, all directors are liable to bear the consequences. Where directors are grossly negligent or knowingly fail to perform their duties, such directors are also liable to third parties or shareholders for the resulting damages. However, if directors can **demonstrate that they exercised their duty of care to the standard of a prudent manager** in the performance of their duties, they will **not be held liable**.

Examples of how directors could breach their duties in relation to climate risks include:

- **Violating** a specific **legal provision**. For example, failing to consider the *Climate Change Adaptation Act,* which requires businesses to endeavour to adapt to climate change in accordance with the content of their business activities.
- **Not establishing** a proper **climate risk-management system** to oversee and manage climate-related risks and opportunities (including both physical and transition risks).
- **Not engaging** in **oversight** of the management of climate-related financial risks. For example, failing to make relevant enquiries to management regarding physical and transition risks to the business due to climate change.
- **Not complying** with relevant provisions of the **Corporate Governance Code**, where the principles have been **adopted** by the company.
- **Not seeking** outside **expertise** where the directors and managers do not possess the knowledge or expertise to devise a strategy to address climate risks.
- **Not robustly assessing** the **assumptions** underlying revenue/cost projections for **climate-related disruption**.
- **Not ensuring** assets and supply chains are **resilient** to foreseeable physical climate risks.

The Corporate Governance Code: reinforcing the duty of care of public companies

Japan's Corporate Governance Code, while non-binding, outlines fundamental principles aimed at fostering effective corporate governance in listed companies across Japan. The 2021 revision of the Code **advocates the adoption of sustainable, long-term business strategies**. The Code recommends that boards develop a basic policy for the company's sustainability initiatives to increase corporate value over the medium to long term. The Code offers **strong normative guidance** for directors to effectively manage material climate-related financial risks and opportunities in compliance with their legal duties. Once **adopted** by a company, directors owe a **duty of care not to ignore the principles** because they should be treated as "fundamentally important internal rules".

Financial materiality of climate risks

Climate risks in Japan

Four years since the original report, the urgency of the climate crisis is increasingly clear, with Japan suffering direct impacts of acute climate events. These include sea-level rise, causing an inundation into fresh water sources that are affecting food production, increased frequency and severity of typhoons, and sustained heat waves causing increasing climate-related morbidity and mortality rates.

> The cost to Japan for climate change-related damages in the decade through 2023 was USD 90.8 billion.

In February 2025 Japan's Cabinet approved the Plan for Global Warming Countermeasures. This plan sets targets for reducing greenhouse gas (GHG) emissions - a 60% reduction from fiscal 2013 levels by fiscal 2035, 73% by fiscal 2040 and net zero by 2050. The target approved for 2035 is a 60% reduction compared to 2013 levels (about a 54% reduction from 2019 levels).

The Bank of Japan has acknowledged that **climate change poses a systemic risk to the Japanese financial system**. It reports that:

- Asset prices could fall as climate-related risks materialise.
- Misevaluation of climate risks can lead to the misallocation of resources.
- The financial system, and thus financial stability, is affected when physical risks and transition risks materialise.

> The G20 *Climate Risk Atlas* reports that Japan stands to lose around 3.72% of GDP by 2050 under a high emissions scenario. An investor led report using central banks data found that Japan GDP loss could reach 10% by 2050 if current global policies continue.

What are climate risks?

Climate risks are the potential negative impacts of climate change on an organisation. They include both physical and transition risks, which themselves are linked. The mismanagement of such risks can create legal risks. Climate risks can have a range of impacts on companies. For example:

Physical risks: Direct damage to assets can **reduce collateral value, disrupt production, and impact supply chains**. These physical risks may lead to balance sheet write-downs, weakened creditworthiness, higher capital costs and increased insurance expenses, affecting **annual revenues**.

Transition risks: Changes in supply, demand, and investor or consumer perceptions of climate risks and opportunities can create **reputational and social risks**, impacting a company's **social license to operate**. Additionally, businesses that do not engage in climate mitigation and adaptation may face **reduced access to capital and increased costs**.

Legal risks: **Policy and regulatory measures** designed to curb activities contributing to climate change, such as carbon pricing, may lead to **stranded assets**. In Japan, legislation like the *Climate Change Adaptation Act* and the *Act on Promotion of Global Warming Countermeasures* establish **regulatory expectations** that all sectors of society must actively make efforts to control climate change through mitigation and adaptation. Japanese directors face **legal risks** if they do not recognise regulatory signals on managing climate-related financial risks or neglect to prevent misleading climate disclosures. Potential claims include:

- Investor lawsuits for breaches of directors' duties (e.g., derivative actions).
- Securities law claims for failing to disclose material climate-related risks.
- Legal actions by regional governments or public interest organisations.

A study published in November 2024 found that climate-related legal filings or unfavourable court decisions led to an average 0.41% drop in stock returns, with carbon majors experiencing declines of 0.57% following filings and 1.5% after adverse rulings. As financial losses from climate change grow, litigation risks for directors who fail to act are expected to rise.

Opportunities with the governance of climate risks

It is not enough to stop at risks. Directors could also be found in breach of their duties and found personally liable for failing to act in accordance with their duty to act in the best interests of the company by failing to address climate-related **opportunities.**

Climate opportunities are the potential **benefits** that an organisation can gain from addressing climate change. For example, taking climate change into consideration in the organisation's strategy can help **reduce costs**, utilise **resources more efficiently** and **build resilience** along the supply chain.

The government's Synthesis Report also discusses the **opportunities that climate change presents**. It uses, as examples, businesses developing information technologies, such as:

- Agricultural support services to project and assess risks from disasters, and technologies to improve the heat-tolerance of buildings and houses.
- Financial instruments that provide insurance or a hedge against possible damage due to abnormal weather events.

There are also **financial opportunities** with the adoption of **effective climate governance structures.** These include:

- Reduced operating costs through efficiency gains (e.g., resource use).
- Improved resiliency along the supply chain.
- Increased production capacity.

Building on these opportunities can result in increased revenues, increased value of fixed assets (e.g., highly rated energy-efficient buildings), increased revenue through demand for lower emissions products and services, increased reliability of the supply chain and the ability to operate under various conditions.

Climate-related disclosures

Disclosure requirements: Japanese companies are increasingly required to disclose climate-related risks. Since April 2022, Taskforce on Climate-related Financial Disclosure (TCFD)-aligned disclosures have been mandatory in the Tokyo Stock Exchange (TSE) Prime Market. All **listed companies** (approximately 4,000 companies, including foreign companies listed in Japan) have had to **disclose sustainability information** generally aligned with the TCFD, since January 2023.

The International Financial Reporting Standards (IFRS) are one of four permitted financial reporting frameworks in Japan. In June 2023, the IFRS' International Sustainability Standards Board (ISSB) finalised two new disclosure standards, effective 2024: general requirements for disclosure of sustainability-related financial information (IFRS S1) and climate-related disclosures (IFRS S2). These standards have absorbed the TCFD framework.

The SSBJ was established to develop the standards to be applied in Japan. The SSBJ issued its final standards on 5 March 2025. From this date, companies may **voluntarily** apply the standards. It is expected that they will eventually become **mandatory** under Japanese securities law and regulations for companies listed on the TSE Prime Market, potentially starting March 2027.

Among other things, it should be noted that the SSBJ's final standards require the company to disclose:

- Scope 1, 2 and 3 GHG emissions (noting that transitional provisions exempt companies from Scope 3 disclosures for the first fiscal year of reporting).
- Climate-related transition risks.
- Climate-related physical risks.
- Climate-related opportunities.
- Capital deployment.
- Internal carbon prices.
- Climate-related considerations in remuneration.

Discussions are underway regarding the scope of additional companies required to disclose under the SSBJ standards, the standards and level of assurance, and the establishment of an assurance system.

Duty to disclosure material information: The duty to disclose is embedded in the *Financial Instruments and Exchange Act* (FIEA)*.* The FIEA contains the duty for all **publicly listed** companies to disclose, on a continuous and periodic basis, material business risks. This requirement includes material business risks arising from climate change.

The *FIEA* requires listed companies to fairly disclose information to investors. This **fair disclosure rule** applies to information of a precise nature that, if disclosed, is likely to have a **material influence** on the value of securities and investor investment decisions. Such information must be promptly disclosed.

In addition, directors of both **privately and publicly held** stock companies in Japan have an obligation to shareholders to **report material financial information in their financial statements**.

Climate change presents a foreseeable financial risk in the short, medium, and long term. As such, **directors have a responsibility to disclose material climate risks.**

Directors also have duties in relation to **forward-looking information**, including information on the impact of **climate-related risks**. Directors may be held liable if it fails to disclose material forward-looking information that could affect investors' decisions where the management was **aware** of the information as of the filing date and **withheld** such information, and also where management was **not aware of the materiality** of the information without reasonable grounds.

Non-compliance: Directors have the **overall responsibility** for ensuring the company's financial disclosures are accurate. Therefore, they may be **primarily liable** for **misleading disclosures** made to the

market. Both **companies and directors** may be subject to **sanctions** under financial services legislation for failure to comply with disclosure requirements. For example, a person who submits an annual securities report that either lacks material information or contains a false statement about a material particular that is required is subject to punishment by imprisonment for not more than 10 years, a fine of not more than 10 million yen, or both.

Unlike general director duties under company law, disclosure pursuant to financial services law is not subject to the business judgment rule, as the requirements are clearly set out in law.

Future trends

Investor pressure

Institutional investors also have **fiduciary obligations to address climate risks**. Certain investors such as pension funds need to consider the **intergenerational impact** of their investment decisions.[6] The Financial Services Agency's *Stewardship Code*, while non-binding, references the responsibilities of institutional investors to enhance the medium- to long-term investment return by **fostering investee companies' sustainable growth** through constructive engagement.

Investor engagement and any decisions to shift investment portfolios towards climate-mitigating activities will directly affect investee companies. If company directors do not **recognise these shifts in capital market** activity, they may be in **breach of their duty of care**. As institutional investors increasingly insist that their investee companies report their management of climate-related risks and opportunities and metrics relating to decarbonisation, disclosure of oversight and management of climate-related risks is likely to generate enhanced corporate governance.

Past shareholder proposals have called for:

- Enhanced transparency in lobbying activities.
- The development of clear, credible and comprehensive transition plans.
- Increased resilience of assets in the face of climate change.
- The integration of environmental targets into executive compensation structures.

These proposals have historically garnered levels of support between 10 to 36%.[7] While no environmental proposals have passed in Japan between 2020 and 2024,[8] shareholder proposals in Japan are expected to increase and become increasingly sophisticated - for example, proposals calling for concrete transition roadmaps and specific, time-bound targets that address climate risk mitigation, emission reductions and a strategic shift towards low-carbon products and services.[9]

Investors have made it clear that climate change is a financial risk that needs to be managed, placing these **proposals squarely within the duties of directors** to undertake oversight and management in the best interests of the company.

Nature

More than half of the world's total GDP is moderately or highly dependent on nature and its services and is therefore exposed to nature loss.[10] Despite this, biodiversity - the variability among living organisms - is being lost at an increasing rate. The average size of wildlife populations has declined by 73% between 1970 and 2020[11] and we are using natural resources 1.7 times faster than ecosystems can regenerate them.[12] If left to continue at current rates, biodiversity loss could cost the global economy USD 2.7 trillion annually by 2030.[13]

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[6] Hiro Mizuno *et al*, Our Partnership for Sustainable Capital Markets (March 2020).
[7] I Tietboehl and J Frank, Japan Shareholder Proposal Landscape 2024: Shareholder Proposals to Focus on Capital Efficiency Long Term Value Creation ISS Corporate (27 May 2024).
[8] White & Case, Japan 2024 Proxy Season (7 November 2024).
[9] I Tietboehl and J Frank, Japan Shareholder Proposal Landscape 2024: Shareholder Proposals to Focus on Capital Efficiency Long Term Value Creation ISS Corporate (27 May 2024).
[10] PwC, Managing nature risks: From understanding to action (April 2023).
[11] WWF, Living Planet Report – A System in Peril (2024).
[12] David Lin et al., Ecological Footprint Accounting for Countries: Updates and Results of the National Footprint Accounts, 2012–2018 (September 2018).
[13] World Bank, The Economic Case for Nature: A Global Earth-Economy Model to Assess Development Policy Pathways (June 2021).

The Taskforce on Nature-related Financial Disclosures (TNFD) has developed a set of disclosure recommendations and guidance that encourage and enable business and finance to assess, report, and act on their nature-related dependencies, impacts, risks, and opportunities, aimed at enabling businesses and financial institutions to integrate nature into decision making. In 2024, the ISSB announced that it will begin work on disclosure requirements relating to risks and opportunities associated with biodiversity, ecosystems, and ecosystem services.

Japan has rich biodiversity and Japan's **capital market and companies face moderate to high dependencies on nature**, especially in the energy, food, beverages, and tobacco sectors.[14] It is estimated that public equities in Japan are particularly exposed to nature-related risks, with **18% of the local stock market's capitalisation** (USD 938 billion) comprised of companies in sectors with a **higher direct dependency** on nature (including the construction, food, beverage and tobacco, agriculture and power sectors).[15] **Biodiversity risks may constitute material financial risks that directors have a duty to oversee**.

Further useful resources for directors

Government and private sector resources are available to support directors in meeting their duties to identify, oversee, and manage climate-related risks and opportunities. These include:

- Practical Guide for Scenario Analysis in Line with TCFD Recommendations (Ministry of the Environment, updated 2023): The guide offers practical examples and useful materials for scenario analysis, with the goal of managing climate-related issues and increasing corporate value at the same time.
- Guidance for Integrated Corporate Disclosure and Company-Investor Dialogue for Collaborative Value Creation, 2.0 (Ministry of Economy, Trade, and Industry, updated 2022): The guidance helps corporate directors and managers communicate key information regarding their business models, strategies, and governance systems as a set of value-creation scenarios to investors, based on integrated thinking. The guidance aims to enhance the quality of corporate information disclosure and company-investor dialogue.
- Code of Conduct for ESG Evaluation and Data Providers (FSA, December 2022): This voluntary code sets principles on matters such as quality of the service of ESG evaluation, managing independence and conflicts of interest, and ensuring transparency of methodologies and processes for the evaluation of companies' ESG activities.
- Practical Handbook for ESG Disclosure (JPX and TSE, March 2020): This handbook supports listed companies in their efforts to improve ESG disclosure and recommends that identification and discussion of ESG issues should take place at the board level, given its oversight role, and should include outside directors. It notes that the board of directors is responsible for oversight of whether the response to ESG issues is being suitably carried out and leading to corporate value creation. ESG issues should be included as part of board discussions on strategy, risk management, and business planning, and the board should monitor and oversee progress towards targets related to ESG activities.
- Transition Plan Guidebook (TCFD Consortium, September 2024); Transition Plan Taskforce Disclosure Framework (Transition Plan Taskforce, October 2023), Disclosure Recommendations (April 2024) and sector guidance; Science Based Targets initiative sector guidance (SBTi): Detailed resources to assist companies setting GHG reduction targets and formulating transition plans.

[14] CCLI/CGI, Directors' Duties Navigator: Climate Risk and Sustainability Disclosures, Japan (Fourth edition, September 2024).
[15] Asia Investor Group on Climate Change, Japan's capital market is exposed to nature-related risks: new research by AIGCC, (June 2024), Japan's capital market is exposed to nature-related risks: new research by AIGCC - Asia Investor Group on Climate Change.

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